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HEARING

BEFORE THE

COMMISSION ON SECURITY AND COOPERATION IN EUROPE

ONE HUNDREDTH CONGRESS

SECOND SESSION

SOVIET TRADE AND ECONOMIC REFORMS:
IMPLICATIONS FOR U.S. POLICY

MAY 10, 1988

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PUBLIC HEARING ON SOVIET TRADE AND ECONOMIC REFORMS: IMPLICATIONS FOR U.S. POLICY

TUESDAY, MAY 10, 1988

COMMISSION ON SECURITY AND
COOPERATION IN EUROPE,
Washington, DC.

The Commission met, pursuant to notice, in room 226 Dirksen Senate Office Building, Washington, DC, at 2:00 p.m., Representative Steny H. Hoyer (Chairman) and Senator Dennis DeConcini (Cochairman) presiding.

In attendance from the Commission: Representatives Jack F. Kemp and John Edward Porter; Senators Frank Lautenberg, Timothy Wirth, Alfonse M. D'Amato and James McClure.

Also in attendance: Mary Sue Hafner, deputy staff director and general counsel; Jane S. Fisher, senior staff consultant and hearing coordinator.

OPENING STATEMENT OF CHAIRMAN HOYER

Chairman HOYER. Good afternoon, ladies and gentlemen. I'm very pleased to call to order this hearing of the Commission on Security and Cooperation in Europe.

I'd like to welcome all of you and, of course, my colleagues today to this Helsinki Commission examination of trade relations between the United States and the Soviet Union and its East European allies.

We are extremely pleased to have with us a very distinguished group of experts to discuss this important and expanding facet of East-West relations.

The Commission has scheduled this hearing because of the increased attention that the commercial aspect of East-West relations is getting.

But trade policy is not formulated in a political vacuum. The Helsinki Final Act is a finely crafted document that explicitly sets forward, as political goals of each of the 35 signatory states, progress in the area of human rights and fundamental freedoms, along with increased cooperation in areas of trade, exchanges and military security.

Balance among the different aspects of East-West relations is not, and I emphasize "is not," a rhetorical U.S. goal. It is a stated political objective of all the signatories.

I believe that we can effectively direct our trade policies to address our security needs, our human rights concerns, and our eco-

nomic goals. The potential benefits are enormous. But to avoid the potential pitfalls we must ensure that we carefully construct responsible policies and conduct constructive commercial relations.

However, I might point out that there is a great deal of congressional concern as to how fast we may be proceeding with our trade relations with the Soviet Union and what official government policy may be.

I bring to your attention a letter to Secretary Verity. And I apologize, Mr. Secretary. This is a recent letter, and you apparently have not received it yet. But I think it was sent the latter part of last week, but I'm not sure that we didn't have it sent around for signing. It was signed by 19 of my colleagues, many of whom sit on the House Foreign Affairs and Ways and Means Trade Subcommittees.

In it, they state, "While you," meaning you, Mr. Secretary, and other administration's officials, "have stated the official policy is still one of support for current restrictions on United States-Soviet trade."

"We are inquiring whether the administration has any intentions of amending or modifying these restrictions." Specifically, they refer to the Jackson-Vanik and Stevenson amendments to the Trade Reform Act.

Mr. Secretary, that letter was dated May 5. But, as I said, apparently, you haven't had the opportunity of seeing it yet.

Seated before us today, first of all, Secretary Verity, and a group of witnesses imminently qualified to address the congressional concerns which I have stated, as well as other aspects of East-West trade relations.

Our first distinguished witness to speak today will be Secretary of Commerce Verity. Before I introduce the Secretary, however, let me now turn to the Cochairman of the Commission, Senator DeConcini of Arizona——

Cochairman DECONCINI. Mr. Chairman?

Chairman HOYER [continuing]. For any comments he may want to make.

STATEMENT OF COCHAIRMAN DeCONCINI

Cochairman DECONCINI. Mr. Chairman, thank you. I welcome the Secretary, and I ask that my statement be included in the record. I only want to say that this is a most timely hearing, as the Chairman has said.

I think a significant expansion of trade without proportionate implementation by the Soviet Government of laws and regulations, which, at the very least, allow free emigration for the Soviet people, betray the Helsinki principles that we are here to really talk about.

I'm concerned about this great Nation, about believing that we can proceed with substantial enhancement of trade and not see a change in the laws and a compliance by the Soviet Union. I hope the Secretary can address that today with us.

Thank you, Mr. Chairman.

Chairman HOYER. Thank you. Next, I would like to recognize Senator Al D'Amato from the State of New York, the ranking Re-

publican member of the Commission on the Senate side and also the immediate past Chairman of the Commission.

Senator D'Amato?

STATEMENT OF SENATOR ALFONSE D'AMATO

Senator D'AMATO. Thank you, Mr. Chairman. Mr. Chairman, I want to congratulate you for calling these hearings. And I'm going to ask that my entire statement, Mr. Chairman, be included in the record as if read in its entirety.

I would like, Mr. Chairman, to take this opportunity provided by Secretary Verity's presence here today, and it's one that I particularly welcome, to say a few words.

Mr. Chairman, I opposed Secretary Verity's Senate confirmation on the basis of his past remarks regarding the relationship between human rights and United States-Soviet trade. At that time, he gave assurances of his support for the President's policies on emigration and on human rights.

Having had the opportunity to see what occurred on Secretary Verity's April visit to the Soviet Union, I can say that he is a man of his word. He took a strong public stand for the principles embodied in Jackson-Vanik, that there can be no marked improvement in United States-Soviet trade relations until the Soviets keep their international commitments concerning emigration.

Mr. Secretary, let me say I appreciate the stand you took on behalf of supporters of human rights here in our country, in Israel, in the Soviet Union, and around the world.

And I thank you for your good efforts and say that I am pleased and delighted that you have adequately dealt with any fears and concerns that I may have had, and you have demonstrated the kind of commitment I think we all looked for.

Thank you, Mr. Chairman.

Chairman HOYER. Thank you, Senator. At this time, again, I want to introduce Secretary Verity, our Secretary of Commerce. He recently led a high-level trade delegation for talks in the Soviet Union. Therefore, his testimony is particularly timely.

He has been a point man of the administration efforts to address trade relations with the Soviets and East Europeans and will discuss administration approaches and outline the balance between national security, economic, and human rights interests.

Again, Mr. Secretary, on behalf of all of us, we welcome you to the Commission and look forward to your testimony.

STATEMENT OF HON. C. WILLIAM VERITY, JR.

Secretary VERITY. Thank you, Mr. Chairman. I'm really very happy to be here. I've looked forward to this. I hope I can, as the Senator D'Amato just said, dispel any further fears that you may have.

I have a prepared statement which I'd like to read, and I will read it quickly.

I am pleased to be here this afternoon to discuss Soviet trade, Soviet economic reform, and how they relate to U.S. interests.

I recently returned from Moscow, where I cochaired the 10th session of the Joint U.S.-U.S.S.R. Commercial Commission together

with Soviet First Deputy Minister of Foreign Economic Relations Kachanov. I also had talks with senior Soviet officials, including General Secretary Gorbachev.

It was my privilege to lead a very fine U.S. delegation that included Undersecretary of State Wallis, Undersecretary of Commerce Freedenberg, and other officials from the Departments of Agriculture, Commerce, State, and Treasury; as well as senior officials from the National Security Council and U.S.T.R.

I have a number of documents from the Commission meetings which, with your permission, Mr. Chairman, I would like at this time to submit for the record.

Chairman HOYER. Without objection, they'll be included at the appropriate point in the record.

Secretary VERITY. I would also like to make some brief remarks on my meetings, particularly on their relationship to human rights and emigration.

Our delegation had two objectives. First, to reiterate that fundamental improvements in our trade relationship with the U.S.S.R. depend upon further improvements elsewhere in the bilateral relationship, especially in human rights and emigration; and, No. 2, to seek specific improvements in market access for U.S. companies in the Soviet Union. We believe we achieved both goals.

Let me stress that we did not go to Moscow to make any trade breakthroughs. That was not our purpose. We went to show our interest in growing trade relations and to carry out the President's and General Secretary's instructions from the December summit to develop concrete steps to expand trade and economic relations.

At the forefront of all my discussions were Soviet obligations on human rights. I made it clear that we will continue to relate improved trade relations to emigration and that the United States cannot extend most-favored-nation tariff treatment, official trade credits, or a trade agreement with the U.S.S.R. in the absence of sustained and substantial emigration from the Soviet Union.

In all my meetings, I urged them, front and center, to adopt policies allowing free emigration and by backing them up with increased emigration.

When Soviet officials raised their interest in MFN, I met this head on. I agreed with their analysis that without MFN they would not be able to sell much in the U.S. market and told them that the ball was in their court.

I suggested that they apply *glasnost* to emigration; that is, that they implemented procedures for free emigration. I stressed this was the only way to get most-favored-nation treatment in the U.S. market. I told them that Jackson-Vanik represented the will of the American people and would stay on the books. The United States is a nation of immigrants, and the right to emigrate is one that is held dear by all Americans.

I emphasized that the United States viewed bilateral trade as an important part of the overall relationship with the U.S.S.R. We could not separate trade from the rest of the relationship.

I told them I came to explain U.S. interests and to seek areas in which Soviet interests and U.S. interests converged. I told them that I hoped they would decide on open emigration policies for their own internal reasons of *glasnost*.

Emigration has generally not been seen by the Soviets as being in their interest over the years. But many things are changing in the Soviet Union, and perhaps Soviet views on emigration are changing as well. If that is the case, then this could have an extremely beneficial effect on our trade relations.

There have been some changes in Soviet attitude. As one indicator, Jewish emigration from the U.S.S.R. last year was about 8,000, roughly eight times the average of the last 4 years. While this is still considerably below the levels of the 1970's, it nevertheless represents a real step forward. I told Soviet officials that I found this development encouraging, that it was a good beginning, and that I hoped it represented a trend that would continue.

Another encouraging development is the joint statement that First Deputy Minister Kachanov and I issued at the end of the Joint Commission meeting. This is included among the documents I am submitting for the record, but I would like to read one part,

> The Governments of the United States of America and the Union of Soviet Socialist Republics recognize that the prospects for a substantial expansion of trade relations are related to progress on other issues of mutual interest, including humanitarian affairs.

This is the first time that a joint statement of both Governments has acknowledged the reality of this relationship.

Mr. Chairman, let me turn to our second objective in Moscow, obtaining better market access for U.S. firms. While stressing that fundamental changes in our trade depend upon progress in the rest of the relationship, I also emphasized our interest in step-by-step, concrete, progress in trade and economic relations within present U.S. policy.

Our goal was to improve market access and market information for U.S. firms seeking to sell in the Soviet Union, sort of a "marketing *glasnost*." This is particularly important as trade authority in the U.S.S.R. is now decentralized to around 100 different Soviet ministries and enterprises.

We agreed in the Joint Commercial Commission on some pragmatic steps which will be of genuine significance to U.S. companies. These appear also in the documents that I am submitting for the record.

To summarize these, we received Soviet agreement to provide us with marketing and purchasing information, to streamline their decisionmaking and cut the time needed for decisions, to initiate a legal seminar series to examine business law and joint venture practices in the Soviet Union, to encourage Soviet buyers to use the U.S. Commercial Offices, and to form working groups to develop trade in food processing equipment, oil and gas equipment, construction equipment, medical equipment, and consumer goods equipment.

These are significant gains, particularly when added to the earlier steps we started taking in 1985. We also signed a protocol amending the Long Term Economic, Industrial, and Technical Cooperation Agreement between the two countries. The main purpose of this protocol was to recognize the new forms of business organization, such as joint ventures, now permitted in the U.S.S.R.

In talking about trade expansion, we must be realistic. Total United States-Soviet trade is a small part of both countries' total

commerce. Last year, our $1.5 billion of exports to the U.S.S.R. were only one-half of 1 percent of U.S. exports to the world. They were only 4 percent of OECD exports to the U.S.S.R., meaning that Europe and Japan accounted for about 95 percent of Western trade with the Soviet Union.

And I might add that our nonagricultural exports to the U.S.S.R. last year amounted to 2/100ths of 1 percent of the Soviet Union's GNP.

Soviet economic restructuring and foreign trade decentralization should open new opportunities for bilateral trade expansion. For instance, we are aware of a number of American companies that are interested in exploring the commercial potential of joint ventures.

As both countries' leaders noted in their joint statement concluding the 1987 summit, commercially viable joint ventures that comply with the laws and regulations of both countries can play a role in the expansion of commercial relations.

However, having a role does not mean having the only role. We should not discourage companies and enterprises from entering into mutually beneficial joint ventures that comply with U.S. law. But we must also ensure that forming a joint venture does not become a requirement for a U.S. company to gain access to the Soviet market.

The President and General Secretary Gorbachev have endorsed the expansion of nonstrategic trade, and this support was reaffirmed in my meetings in Moscow.

But let me stress that U.S. export controls were not on the table for discussion. Our national security requirements remain paramount. Strategic goods and technology are not areas where we are, or will be, interested in trade expansion with the Soviet Union. Export controls are not a barrier to trade expansion in legitimate nonstrategic areas. In addition, we have not changed our position opposing Soviet membership in the GATT and other international economic institutions.

While Soviet trade and economic reforms increase the potential for trade, the major factors affecting United States-Soviet trade remain. Progress in trade will continue to be related to progress in the overall United States-Soviet relationship.

Additionally, we believe that trade with the U.S.S.R. needs to be approached with realism and sound commercial calculation, neither exaggerating nor minimizing opportunities and benefits for either side.

We believe our policies provide for mutually beneficial expansion of trade in a way that will allow trade to contribute to the overall United States-Soviet relationship. There are areas in which trade can be expanded now, and it is the administration's policy to encourage and promote that expansion.

These basic policies do not lay out an easy course. They are, however, policies which we believe are realistic and which provide a solid basis for carrying out a consistent, principled, long-term policy which is understandable to Americans, the Soviets, and our allies.

Mr. Chairman, that concludes my statement. I will be pleased to answer any questions the Commission may have.

I might add, Mr. Chairman, that one of the things we learned today that may be of interest to this group——

Chairman HOYER. You're anticipating my first question, I think, but go ahead.

Secretary VERITY. I'll put it in your court.

Chairman HOYER. We're very pleased about that.

Secretary VERITY. It's much better if you ask the question.

Chairman HOYER. All right. That's fine. Mr. Secretary, first of all, I want to thank you for your statement.

Second, my first question is, as you know, the law establishing the Commission on Security and Cooperation provides for both Senate and House membership, and I, in this group here, need to stress that it's a bicameral Commission, although I'm very significantly outnumbered today.

It also provides for representation from the State Department, from the Defense Department, and from the Commerce Department.

Now, Mr. Perle, who was the Commission representative of the Defense Department, is here today. Unfortunately, his vacancy has not been filled. Mr. Schifter, Assistant Secretary of State for Human Rights and Humanitarian Concerns, is a very active member of the Commission.

But we have not had representation from the Commerce Department. I would like to ask you—and I know the answer to the question and am pleased with it, but I would like to ask you the status of that.

Secretary VERITY. Well, Mr. Chairman, we are happy to say that the President intends to appoint Assistant Secretary Laun as the Commerce Department's representative on this Commission on Security and Cooperation in Europe.

We thought that the President might do that today. We're now told that the President will do this tomorrow. So we're very happy to have Secretary Laun join this distinguished group, and I think you'll find that he'll be a very committed member.

Chairman HOYER. Thank you very much for that and please express our pleasure with the President's decision to make the appointment. Mr. Laun is in the room, in the hearing room, with us. We look forward to his being appointed and his service on the Commission. We think that's a step forward, particularly at a time, as I said in my opening statement, where Basket II is going to be very much a focus of the Commission.

Before going forward and asking questions, let me recognize additional members of the Commission who have joined us; first, Senator James McClure from Idaho. Senator, would you like to make any statement?

Senator MCCLURE. No. I have no statement.

Chairman HOYER. All right.

Senator MCCLURE. I do have a few questions.

Chairman HOYER. To my left, Senator Tim Wirth, from Colorado, and to his left, Senator Frank Lautenberg from New Jersey, both members of the Commission. All of the Members here are members of the Commission.

Mr. Secretary, you mentioned in your testimony that you suggested to the Soviets that they apply *glasnost* to emigration policy.

What was their response? What was the substance of the discussion that you had with reference to that suggestion?

Secretary VERITY. Well, I mentioned that, Mr. Chairman, twice. I mentioned that many times, but I thought you would be particularly interested in two replies that I first got from Prime Minister Ryzhkov, who was the first minister I met on our trip. And, by the way, there were other members of our delegation with me.

Prime Minister Ryzhkov listed six items that he wanted to talk about, and one of them was MFN. And I covered all of the items and got to MFN last and made the point that I had been hearing a lot about *glasnost*; and that I felt that it was up to me at this particular time to point out that if the Soviets wanted MFN and that we in the United States felt that it was important to get MFN at some time if we're going to have substantial trade between our two countries, that, heretofore, they had blamed us for not being able to get MFN; that I felt that the ball was in their court. If they wanted MFN, what they should do is to apply *glasnost* to emigration, which, to me, meant openness. If they would open their emigration, no quotas, no family permission, after 5 years that the person had been in a sensitive position, they should then be free to emigrate. I reminded him that the law of our land was the Jackson-Vanik bill, that that was not going to go away, and that we are a land with immigrants. This wasn't just important to the Jewish group, but this was important to all of America; and that I felt the time had come for him to understand that, if they wanted to do something about it, it was up to them.

Prime Minister Ryzhkov said, "I didn't think you came here to talk about things that happened back in 1972 or 1973 or 1974" and sort of started to put it under the rug.

I said, "No, Mr. Prime Minister, I didn't come here to deal in past history. You had on your list of things, 'MFN.' And, if you want to know how I think you can get MFN, I've just explained it because the only way I know you can get MFN within our laws is to take advantage of this moment of *glasnost*, apply it to emigration."

And I said, "I think, if you would do that, and if it were announced, and if figures, emigration figures, indicated that you were carrying out such a policy," I said, "I think that our President, our Congress would all look favorably upon a waiver after a period of months which would provide that this was happening with the waiver."

And I said that's the only way I know that they were going to be able to lick this problem. General Secretary Gorbachev asked me the same question. And when I gave him the same answer that I've given you, he chided me and said, "I don't think we ought to talk about matters of internal affairs. I don't think that you're here to talk about what the Soviets should or should not do."

And I said, "Well, Mr. General Secretary, I did not come to talk about those kind of things. That's not my position. I'm here to talk about commerce and trade. But you asked the question on MFN, and I've given you the honest answer that I know."

And he said, "Well, do you think there's a chance to get MFN in this administration?" And I said, "I doubt it very much." And he said, "Why is that?" And I said, "There isn't enough time, that I

don't see, unless something would happen very quickly, that there could be sufficient progress in the figures that would allow that to happen."

And he proceeded on that, wanted to know, "Well, what kind of time?" and so forth. And then he wanted to know, if he would do something promptly, could it happen?

And I said, "Well, Mr. General Secretary, I don't know what's on your mind, but if you would come out with such a statement and then the figures would start to show great improvement," I said, "I think it would be seriously considered by the people of the United States."

That was the end of the conversation.

Chairman HOYER. I guess one could say, in shorthand, that meeting the Helsinki Final Act obligations and undertakings would have a——

Secretary VERITY. I didn't mention that to General Secretary Gorbachev. I did with Prime Minister Ryzhkov, that what we would really be doing is living up to the signature that they had placed on the Helsinki Agreement.

Chairman HOYER. Mr. Secretary, I've got a lot of questions I want to ask. Two brief ones, because I've got so many of my colleagues here. You mention in your statement "nonstrategic trade."

Can you give me the administration's or the Commerce Department's definition of "nonstrategic trade?"

Secretary VERITY. Well, I'll be happy to give you my description, and I have with me Undersecretary Freedenberg, who's in charge of export administration and can answer any specific questions that you may have.

By "nonstrategic trade," we're talking about, principally, products that are being freely traded now with the Soviet Union by our allies.

And during our meeting of the Joint Commission, in order to focus on nonstrategic trade, we talked about five particular areas, and the areas we were talking about were food processing equipment, construction equipment, medical equipment, et cetera—I'll be happy to give you further details on that—oil and gas equipment.

We're talking about items that have to do with improving the life of the consumer in the Soviet Union rather than in any way improving their military capability.

We certainly are against that. We made it clear to the Soviets during our discussions with them, and never once did we get into any high technology or any controlled items.

So, to me, "nonstrategic" means just that. It's products aimed at improving the life of the consumer in the Soviet Union. We don't feel that it endangers our military security.

And most important, as far as I'm concerned, these items are now being sold in great amounts, $25 to $40 billion a year, by our trading partners, of which we're getting a very, very minor part.

Chairman HOYER. Thank you, Mr. Secretary. If you want to amplify that answer, that would be fine later on. It's not required, but if you wanted to do that in writing, that would be fine.

Secretary VERITY. I'll ask my expert to—we'll be happy to put anything further in the record.

Chairman HOYER. Fine. Mr. Secretary, I've been requested to ask you to move the microphone a little. We can hear you fine, but I'm not sure everybody in the back of the room can hear you as well.

Thank you, sir.

Secretary VERITY. Is that good or bad?

Chairman HOYER. I guess it depends upon the perspective of the listener and the substance of the answer.

Secretary VERITY. Yes, sir.

Chairman HOYER. Senator DeConcini?

Cochairman DECONCINI. Mr. Chairman, due to the time restraints here, I'm going to limit my questions likewise. I do want to ask Secretary Verity, do you feel the Jackson-Vanik amendment has been effective?

And what is your position—or the administration's position regarding the continuation of this type of amendment?

Secretary VERITY. Of Jackson-Vanik?

Cochairman DECONCINI. Yes, sir.

Secretary VERITY. Well, I think Jackson-Vanik is a—was the will of the Congress in 1974. It's been in effect that long. And now it's sort of a part of the scenery that isn't going to go away.

Cochairman DECONCINI. Has it been effective, in your opinion?

Secretary VERITY. I'd have to say that I don't think it has been effective.

Cochairman DECONCINI. Thank you.

Secretary VERITY. And I never felt that this is the way to——

Cochairman DECONCINI. At what point would you favor the exercise of the President's waiver authority under that law?

Secretary VERITY. I want to make it clear, Senator, that I am not for repealing Jackson-Vanik.

Cochairman DECONCINI. I understand.

Secretary VERITY. My belief is that the waiver should take place when we are convinced that the Soviets are serious about opening up emigration and, through a trend, or whatever else you want to use, are making it clear that their opening up of emigration is working, and that those people who want to emigrate are allowed to emigrate.

Cochairman DECONCINI. And last question. Mr. Secretary, prior to becoming Secretary, you've dealt in the private sector with the Soviet Union.

What kind of items do you think—if most-favored-nation status was given or approved for the Soviet Union, what kind of items do you think would be most acceptable in the United States? Have any surveys been done?

Secretary VERITY. Well, we talked about——

Cochairman DECONCINI. Any information along that side besides outstanding vodka?

Secretary VERITY. Well, I think the problem now, as you know, Senator, is one of tariff. Without MFN status the Soviets are penalized to the tune of 25 to 35 percent.

When they would try to ship a product in here with that kind of a——

Cochairman DECONCINI. I understand. But if most-favored-nation status was granted, what would be the products that you think we would see?

Secretary VERITY. I think what they would do is try to concentrate on two or three different areas where they could produce a quality product that would be purchased by Americans.

That would be in the machinery area. We already are getting things in fuel and nonferrous metals. But it would be those kind of things.

They once tried small trucks. Our people considered them junk. If they would produce a good small truck and concentrate on it, I think they could probably ship that kind of a product into this country.

That's only an example. There are——

Cochairman DECONCINI. Yes. I just wondered if there was any idea from the Commerce Department just what kind of items we might anticipate and if you would like to supply that to the record, if, in fact, you've done any surveys or what have you.

Secretary VERITY. If we've made them. I'll ask my colleague.

[Whereupon, Secretary Verity confers with colleague.]

Secretary VERITY [continuing]. Well, Frank Vargo, who handles this area, says we have not made such a survey for some time.

Cochairman DECONCINI. Are there other items besides trucks that you would guess might be imported by the United States?

Secretary VERITY. Well, I was thinking of machinery items. The Soviets are pretty good at some of that.

Cochairman DECONCINI. Thank you.

Secretary VERITY. And if they could find one that they thought was of interest and they concentrated on it, I think they could probably sell some here.

Cochairman DECONCINI. Thank you.

Mr. Chairman, I'll yield. I have other questions, but due to time.

Chairman HOYER. Senator D'Amato?

Senator D'AMATO. Oh, Mr. Secretary. After I said all those nice things, too. Mr. Secretary, do you know if the President plans to ask for waiver of Jackson-Vanik in connection with the Moscow summit? Have you heard anything about that?

Secretary VERITY. I don't believe there is any plan, Senator, for the President to do anything about a waiver at the summit. I think there's a possibility that if Secretary General Gorbachev would bring up the subject of most favored nation, which he may, I think the discussion would then be that, "Yes, that is possible under a Presidential waiver. And, in order for that to happen, this is what would have to happen as far as emigration is concerned."

I would hope that might happen. But I do not know of any plan at the moment that says it will happen.

Senator D'AMATO. Mr. Secretary, let me just touch on one other thing. This Commission, over a period of years, has heard extensive testimony regarding the use of forced labor and Soviet production for export.

Do you support enforcement of section 307 of Smoot-Hawley? And could you provide the Commission, for the record, with the Commerce Department's position on the standards that must be met to show that forced labor was involved in the production of goods to the extent that section 307 should be triggered?

Secretary VERITY. Well, Senator, this is a problem that seems to me would require a lot more proof than anyone has come up with yet as to forced labor.

This is an item that one member of our delegation mentioned in our meeting with Prime Minister Ryzhkov. And Prime Minister Ryzhkov turned the tables on us and said, "Are any products in the United States produced by prisoners and sold by them?"

Well, it seemed to me that this was a pretty unproductive subject to talk about, and we didn't go any further; so that it seems to me, to get into the subject of forced labor, it's going to take a lot more proof than I am aware of.

Senator D'AMATO. Well, let me just ask you if you wouldn't, for the record, provide the Commission the Commerce Department's position on the standards that must be met to show that forced labor was involved.

I think at least we'd begin to make some progress if we can look at that pursuant to section 307.

Secretary VERITY. I'm not that familiar with the details, but I'm told that we'll be happy to supply you the test that we're now using.

Senator D'AMATO. Good.

Secretary VERITY. Would that be satisfactory?

Senator D'AMATO. I'd be—that's exactly what we're asking.

Secretary VERITY. Fine.

Senator D'AMATO. I'd appreciate it. Thank you, Mr. Chairman.

And thank you, Mr. Secretary.

Chairman HOYER. Senator McClure?

Senator MCCLURE. Thank you very much, Mr. Chairman.

I appreciate the comments that you've made with respect to your negotiations and your conversations with the Soviets when you were there. But it seems to me, if I understand you correctly, you're kind of erecting one single standard with respect to MFN. And that's numbers on emigration.

Am I correct in that assumption from your testimony?

Secretary VERITY. Senator, I don't know that it's necessarily numbers. That has been the way that various groups have made judgments as to whether or not they're reaching a satisfactory level.

Senator MCCLURE. Well, they were, at one time, up to around 50,000 a year. There are some who are speculating that this year, with the Armenian crisis and the possibility that they may expel Armenian dissidents, the numbers might go way up again, based simply upon that one political development in the Soviet Union.

That would change the numbers without really changing fundamental policy, wouldn't it?

Secretary VERITY. Well, the emigration figure that I am discussing, that 8,000, are refuseniks, or the Jewish people being emigrated from the Soviet Union.

Actually, the amount of emigrants to Germany is around 10,000. And in the Armenian figure, I understand it was about 8,000 itself.

So I don't know what the total is. I was talking about this one particular thing that Jackson-Vanik addresses; and that is, the freedom of the Jewish people who care to emigrate to be able to emigrate from the Soviet Union.

Senator MCCLURE. Well, that's the reason I asked the question. It seemed to me your statements were really pretty much confined to that one issue. That's what I'm trying to find out, whether or not you have in your mind only that single issue with respect to our willingness to consider granting MFN. Or is there a broader range of issues that they would have to address before we're ready to talk about MFN?

Secretary VERITY. Well, Senator, we talked about that before we left because the whole expanse of human relations et cetera, means different things to different people.

In the case of Jackson-Vanik, it focuses on emigration.

Senator MCCLURE. On one aspect of emigration in practice. An important aspect, but in practice, one aspect of emigration.

Secretary VERITY. Well, it's the one that we felt if we focus on that particular item, they know what we're talking about, and we are——

Senator MCCLURE. Well, I'm not sure that they know, because I'm not sure that I know what you're talking about. And I'm not necessarily more dense than they are.

That's the reason I ask the question, because I look at page 2 and page 3 of your prepared statement, I listen to the answers that you've given, and, in each instance, you're talking about, "You can't get to MFN status until you've addressed Jackson-Vanik, unless you've aggressed emigration in the context of Jackson-Vanik."

And there are broader issues of emigration than that, are there not? There are broader issues of human rights than simply that one standard? Am I not correct?

Secretary VERITY. Well, there are certainly broader issues in human rights than just emigration. If you're talking about just emigration, it seems to me that there are two things involved.

One is openness in the sense that you will allow people to emigrate.

The second thing that would require the issuance of a waiver would be that if the quantity was sufficient to encourage the Congress and the President to feel that they were doing what we had hoped they would do in emigration.

So you have the two things, openness and numbers. And I don't know which is the most important.

Senator MCCLURE. Well, again—and I don't mean to belabor the subject—the Helsinki Final Act, the accords that were signed by 35 countries, address a broader range of human rights issues than the single issue of emigration.

I was in the Soviet Union very recently, and met with members of the Supreme Soviet and other officials. I told them I would be much more impressed if, rather than simply increasing the numbers of refuseniks allowed to leave by the several thousands that we are hoping for—and that's an important issue, and I hope they'll do it—they would tear down the Berlin Wall.

Now, why can't we talk about observance of the agreements that they signed at Helsinki, which are broader than the single issue of emigration? For example, we have the question of the treatment of the Helsinki monitors inside the Soviet Union.

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I had the opportunity to talk for 1½ hours one evening with Dr. Sakharov. He's not a refusenik. He doesn't seek to emigrate. He does seek to expand the observance of human rights within the Soviet Union, areas that were guaranteed in the Helsinki Final Act. And it seems to me that if we are really behind the Helsinki Final Act, as we should be, then we ought to be talking about MFN in return for progress on a much broader range of human rights issues than simply emigration and compliance with Jackson-Vanik.

Secretary VERITY. I don't disagree with what you're saying, Senator.

Senator MCCLURE. Then I would assume you would have no objection to legislation forbidding the President to grant MFN status to any signatory of the Helsinki Final Act not currently receiving MFN treatment, unless he can certify that that country is in full compliance with the provisions of the Helsinki Final Act?

Secretary VERITY. I have no objection to it. I think that if we really want to make progress with the Soviets so they understand that they're priority items, I would go to work on the emigration first.

Senator MCCLURE. I don't object to you working on emigration. I just object to stopping there. I understand that we have to be careful about talking about interfering in their internal affairs.

But they're asking us to do something for them. We have a right to expect that they'll at least comply with the agreements that they signed before we grant something that they want so much.

Secretary VERITY. Well, I think this problem is going to be a continuing problem for many years to come. And I think we might be in a better position to have some leverage if we had some trade with them, which we don't have now.

Senator MCCLURE. Well, it's a question of whether you grant it first and hope for the leverage later, which I judge is your approach, or whether we would hope to use the prospect of MFN for leverage, which I favor.

Secretary VERITY. Well, I think we're——

Senator MCCLURE. Thank you very much, Mr. Secretary.

Secretary VERITY [continuing]. I think we're doing the latter.

Chairman HOYER. Senator Wirth?

Senator WIRTH. Mr. Secretary, what did you learn from the precedent of 1979, when there were a lot more than 50,000 people leaving the Soviet Union, and that apparently was not adequate for granting most-favored-nation status? Is that right?

Should we conclude from that that 50,000 isn't enough? What are the criteria for the granting of MFN and the waiver of Jackson-Vanik?

Secretary VERITY. Well, I'd make two comments, Senator. One is that the reason that emigration reached that figure in 1979 was because the Soviets were hopeful that they could get approval of the SALT agreement.

And, therefore, they were "opening the gate," so to speak, and 50,000 people were allowed to emigrate. I personally think it would have been a good idea to have talked about the waiver at that time, that that was pretty good performance.

Senator WIRTH. There was a lot of discussion of the waiver at that time, wasn't there?

Secretary VERITY. I was not involved in anything to do with the waiver at that time, but I feel that it would be wise at some time to throw some carrots out if you do see progress in the Soviet attitude on emigration.

I think perhaps we missed an opportunity there to encourage it. Of course, we lost the opportunity because of the invasion of Afghanistan.

Senator WIRTH. Well that's correct. I was in the Soviet Union in late 1979, and Charlie Vanik was in the crew. And there was a lot of discussion at that time of waiving Jackson-Vanik and granting most-favored-nation status. That was sort of the high point, in September or October 1979, as you point out, right before Afghanistan.

Now, my question is, who sets the criteria? Who makes the policy as to what is adequate or what is inadequate? Who in the administration does that? Do you do that? Does the White House do that? Who does it?

Secretary VERITY. Well, if it's like other things, Senator, a lot of people do.

Senator WIRTH. But, I mean, who——

Secretary VERITY. It would be——

Senator WIRTH. How do we know? Like, when Senator McClure was asking the question. Do you just do it on emigration grounds, or do you do it on emigration plus human rights monitors, or do you do it on emigration, human rights monitors, other symbolic activities?

Do you include Armenians and Germans? Who sets that criteria?

Secretary VERITY. Well, I think it would be an inter-agency effort, the National Security Council, the State Department, Commerce and others would participate in it.

Senator WIRTH. Is there a policy as to what the criteria are? Is there currently an administration policy on that?

Secretary VERITY. I do not know. I have a policy within the administration which——

Senator WIRTH. But you have responsibility for administering it; is that right?

Secretary VERITY. We would have the responsibility to make recommendations to the President as to whether or not we——

Senator WIRTH. "We" being the Commerce Department?

Secretary VERITY. The Commerce Department.

Senator WIRTH. Whether you make recommendations against what policy as to whether or not most-favored-nation status should be granted? There isn't any criteria now; is that right?

Secretary VERITY. There is not any criteria?

Senator WIRTH. So it's very difficult for us even to talk about it if there are no criteria for what counts and what doesn't count or, you know, what—we're sort of dealing in a "Never Never Land."

Maybe we're not. Maybe that's the way we want to have it. Is it? Is that a better position for us to have, is to have it ambiguous like that?

Secretary VERITY. Well, I would agree with you that if we had some criteria, it might make it a lot easier for all of us.

Senator WIRTH. Should we be setting that criteria, or is that something we ought to set for you? If you agree that there ought to be some criteria, and I gather from your answer to Senator

McClure's question, who sets it? How do we get that sort of thing done?

Secretary VERITY. Well, maybe what would be a good thing for us to do, is to make a recommendation as to what we think might be the criteria for consideration of a waiver.

Senator WIRTH. All right.

Chairman HOYER. Will the Senator yield?

Senator WIRTH. Be happy to yield.

Chairman HOYER. Mr. Secretary, if I may. I'd like to observe that I think, in fact, you said in your statement that at least as it relates to the emigration question that Jackson-Vanik speaks to, that the criteria is not numbers, but an open door,——

Secretary VERITY. Right.

Chairman HOYER [continuing]. Which is what you've said in your agreement. "We can't get caught in the catch 22 of numbers," whether it's 50,000 or 100,000 or 250,000. The issue is whether or not the Soviets, who have signed the Helsinki Final Act, which incorporates the International Covenants on Political and Civil Rights which speaks directly to the right to leave and return to one's country.

It seems to me, therefore, Senator, that we do have the criteria which is an open door, at least as it relates to the limited question of emigration.

Because if you play the numbers game, you lose, it seems to me.

Senator WIRTH. I'm not suggesting that we want to play the numbers game, but I think that we would all agree that based on the Helsinki Final Act, we're looking at more than just immigration. We're looking at a variety of other items as well.

And it seems to me that as we try to understand this, if we're trying to advocate to the Soviet Union what it is that we think is important, we ought to have some criteria against which we can state what is important and what isn't important. This is an appropriate thing to do. I don't want to belabor this any further, but I think that we ought to have some kind of a national policy or administration policy or set of goals or set of criteria or something that says what it is that we think is important versus something that we may not think important.

Senator McClure is absolutely right in talking about human rights monitors. I think we place much too little emphasis on that and much too much emphasis on some of the other items. But I think that it would be important to do that, and I just hope that you agree.

Let me ask a final question, if I may. We were going to get a list from you as to what it was that we wanted from the Soviet Union. I gather, from your exchange earlier, that we don't have a list like that. If we're going to have trade, presumably, we ought to have a list of what it is we think we're going to get.

Secretary VERITY. Well, Senator, I don't know of such a list. But before I went to the Soviet Union, I did make the three criteria that I mentioned earlier.

And that is that open emigration, to us, meant just that, that you make the statement that emigration is open; there are no quotas; no family permission is required.

And they've always talked about people in sensitive positions should not be allowed to emigrate. And we put a time factor on that. We said that we felt that after such a person had been out of the office for 5 years, that person should be entitled to emigrate. Now that's the only criteria that I have.

Senator WIRTH. Just a final note. Is it in our interest to have our NATO allies make very large loans to the Soviet Union?

Secretary VERITY. I don't know of any large loans that we have with the Soviet Union.

Senator WIRTH. No. By our NATO allies.

Secretary VERITY. Well, recently, you've read about, either yesterday or today, a loan from West Germany to the Soviets. As I understand it, that's a loan being made by a commercial bank in Germany to the Soviets in order to purchase certain things that Soviets want. It is not backed by the West German Government.

And it seems to me if a commercial bank in Germany would like to do that, that's their business.

Cochairman DECONCINI. Can you answer the question, Mr. Secretary? If you don't mind, Senator Wirth? That's a real good question. If you would yield?

You know, is it to our benefit, I believe that's the question Senator Wirth asked, to have those kind of loans made? Do you have an opinion?

Secretary VERITY. I would think so.

Cochairman DECONCINI. You think it is?

Secretary VERITY. I would think that if a commercial bank in Germany, for the benefit of the German economy, thinks it's a good idea to make loars to the Soviets to sell products to them, and they're willing, the commercial bank, to take the risk.

Cochairman DECONCINI. It's to our benefit.

Secretary VERITY. Therefore, they are creating jobs in Germany. They think this is good. That it is all nonstrategic trade. I think it's a benefit.

Cochairman DECONCINI. Thank you. Thank you.

Senator WIRTH. I'm not making a judgment one way or another. I just want to know if it is our policy? Do we want to deal with a fat Russian or a thin Russian, I suppose is one way of putting it; right? And what is perceived to be our national interest? Are we better served by the former or the latter? I think that's what it comes down to.

And where do we want to go? I'm not sure that there is an answer, but I think it's something that we all ought to be thinking about.

Secretary VERITY. Well, for trade to happen, at the moment, will take hard currency. And, therefore, in the case of the Germans, in order to create hard currency so that trade can take place, they have found a commercial bank that's willing to loan some money.

Senator WIRTH. Thank you, Mr. Hoyer.

Chairman HOYER. Thank you. Congressman Kemp?

Representative KEMP. Thank you, Mr. Chairman. I want to congratulate you, Mr. Chairman, and my colleagues for raising issues with the Secretary that are of interest not only to those of us who are sitting on this side of the table, but indeed, as I found out in the last year, to all of the American people. I just wanted to sug-

gest that it may be very possible, given the fact that MFN represents in a sense, a tariff against Soviet exports to the United States of America, Mr. Secretary, that untied loans from the West are offsetting the cost of MFN. And I wondered if you might want to address that question.

Are we tacitly supporting the idea of expanding untied loans at lower-than-market rates of interest to the Soviet Union to offset MFN as a way of trying to open up and broaden trade with the Soviet Union at this moment in history?

Secretary VERITY. To my knowledge, Congressman Kemp, these are not subsidized loans. The Soviet Union, as far as the Germans are concerned, is a developed country. Therefore, any interest rate involved would be at a competitive rate. So it is not a subsidized rate that is being offered, which makes it, I think, a little different from what you indicated.

Representative KEMP. No. What is your understanding of the rate of interest at which most of these untied loans are being offered to the Soviet Union?

Secretary VERITY. I really can't answer that. I only know from this German loan, because we thought this might come up today, to try to determine what the rate was and was there any subsidy involved? Was there any government guarantee involved? Which we thought you would be interested in.

We're told—and I have to confess I have not seen it—that there are no guarantees involved; that it is a competitive rate; it is not subsidized; it's a loan that would be made at a normal rate for a developed country.

Representative KEMP. That would be interesting because it's my understanding that we are today, in the 1980's, making the type of commercial untied loans to the Soviet Union which are not unlike those made in the late 1970's to other Third World countries.

And I think most people know that a lot of those loans were shoved down the throats of those Third World countries. Could it be possible that the cost of MFN to the Soviet Union is being offset by, if not subsidized rates of interest, at least favorable rates of interest?

Secretary VERITY. I wouldn't think so, but it could be. MFN does involve 25 to 35 percent tariff penalty to a Soviet product. Whether or not that is sufficient to offset what you're talking about——

Representative KEMP. No.

Secretary VERITY [continuing]. I wouldn't think so, but it might.

Representative KEMP. Just for the record, I want to closely identify myself with the remarks made by the gentleman from Idaho in terms of linkage between MFN and trade with the Soviet Union to Helsinki and a change in behavior.

The gentleman from Colorado has referred to the $2.1 billion loan from West Germany—which is untied. I understood this to be at a favorable rate of interest—particularly given what Third World nations are having to pay today just in debt service to Western banks. I wondered whether or not you felt that this weren't part of some overall strategy to try to increase trade.

Let me say parenthetically, I stand second to no one in my belief in a world trading system and removing barriers to exports, but when it comes to trade with nonmarket economies, particularly the

Soviet Union, which has such egregious errors in its treatment of people behind the Iron Curtain and its treatment of the agreement that they signed with the United States at Helsinki, it seems to me that we ought to look at the situation a lot more closely. The questioning in this regard is very, very important to lots of people in our country.

I'm particularly persuaded that we're being tougher on some of our allies, Mr. Secretary, than we are on the Soviet Union at this point. The treatment of our allies, for instance, by this administration—and I have been a strong supporter of the administration—well, I have heard some Asian-bashing, particularly with Taiwan, South Korea, Japan, Singapore.

For instance, the other day, an official of this administration, whose name will go unmentioned, because the name is less important than the fact that he represents the administration, was complaining about the fact that Taiwan was tying their currency to the U.S. dollar.

I had always thought that we were working to try to get countries to achieve some symmetry with regard to their currencies and our conduct of monetary and fiscal policy.

But this administration official was decrying the fact that Taiwan, you know, which represents such a great threat to the United States of America, was really doing us in by tying the Taiwan dollar to the U.S. dollar, and why wouldn't they appreciate their currency against the dollar to help America in its trade imbalance with Taiwan?

I was embarrassed, frankly, not only by the political meaning of that statement, but also by the economics. To suggest that the people of Taiwan ought to put themselves through a deflation in order to help the U.S. trade deficit seems to me to be counterproductive and unfair. That goes for South Korea, as well.

But, to get back to my question. I apologize for the lengthy aspect of it, but the premise is still sound. Are we rushing into Détente 2 in terms of trade with the Soviet Union and at the expense of some of our other trading partners?

If we're willing to expand markets in the Soviet Union, we should be willing to try to do more to expand our markets around the world.

And I wondered why these untied loans are being made with such rapidity at this point when *glasnost* has failed to open up emigration, *glasnost* has failed to improve Soviet treatment of Christians and Jews.

It's pretty shallow to the Polish steelworker in Gadansk, and it's particularly shallow to Armenians and Ukrainians and Georgians, and I just wonder why all this rush to provide credit to the Soviet Union?

Secretary VERITY. Well, Congressman, the amount of trade that we do with Taiwan is significant. It's in the billions of dollars, and the trade deficit with Taiwan this year for the United States will be close to $20 billion. And that is significant.

I don't really get your point because we don't trade with the Soviet Union. We don't have any trade with the Soviet Union. The only trade we have with the Soviet Union is grain.

Now the amount of other trade that we do is $500 million. And that will not increase this year.

The purpose of our mission to the Soviet Union was to try to come up with concrete proposals as to how, over time, step-by-step, there could be an increase of trade between our two countries. But it hasn't happened yet.

Representative KEMP. Mr. Secretary, with all due respect, we do trade with the Soviet Union, and it is minuscule, to be sure. But that's your—one of your reasons for being here is——

Secretary VERITY. That's right.

Representative KEMP [continuing]. To talk about expanding trade. All I was suggesting, in juxtaposition between Soviet trade and Taiwan trade, a $20 billion deficit is not prima facie evidence of being an enemy of the United States of America.

Sure, we want to open up more markets in Taiwan, but I am suggesting that the question of untied loans to the Soviet Union, coupled with bashing Taiwan and South Korea for failing to appreciate their currency against the dollar, seems to me to be counterproductive. It's certainly inconsistent with my understanding of the progress towards human rights and democracy in Asia vis-a-vis the Soviet Union.

I just wonder if we are rushing toward a Détente 2 with the Soviet Union at the expense of progress and on behavioral fronts alluded to by every member of this Commission, Democrat and Republican?

Secretary VERITY. Well, I, for one, Congressman, am very anxious to open trade with any country. I think that the amount of trade we're doing with the newly industrialized countries is wonderful.

What has happened in helping build the economies of Taiwan, South Korea, Singapore, Hong Kong, Indonesia and others, is something that I think that this country can be proud of. And the amount of trade we're doing with them is something that is important to their economy and to ours.

I guess the interest that we had in going to the Soviet Union was to try to see if over time we couldn't increase trade with the second biggest market in the world.

And we're behind our allies, who are doing a tremendous amount of business.

Representative KEMP. Mr. Chairman, my only point was, it is being subsidized.

Secretary VERITY. The loan is not subsidized.

Representative KEMP. Sure, it is. The grain is being subsidized.

Secretary VERITY. Yes, the grain that we ship them is subsidized.

Representative KEMP. And it's also being subsidized by untied loans that are helping to meet the capital demands and credit demands of the Soviet Union. Their economy is a basket case. Let's not bail them out, Mr. Secretary.

Let's make them compete in the open market and force a behavioral change in the Soviet Union that's been a long time coming. And I want to identify with that bill to provide some link between MFN and Soviet compliance with Helsinki.

I thank you for your time, and you, Mr. Chairman, for your longtime struggle in this area.

Chairman HOYER. Thank you very much. Congressman Porter? And I might say that we've got four very distinguished, very able people that we want to follow up with, so if we could—we have one also testifying, but we have four additional ones as well.

Secretary VERITY. I got the message.

Representative PORTER. Mr. Secretary, I want to explore the other side of what my colleague from New York raised; and that is, if we had seen some greater willingness on the part of the Soviet Union under Mr. Gorbachev to be forthcoming on some of the things that concern us, some of the values that concern us, particularly on human rights, don't we have to worry about the risk that, if Mr. Gorbachev is not successful in some of the things that are of concern to him in his own domestic economy, particularly, and that might include arms control, that Mr. Gorbachev may well be gone and we will be back to the hard-liners that never were forthcoming on anything that concerned us?

And how do we balance these two risks one against the other and succeed? What are your thoughts?

Secretary VERITY. Well, my belief is that General Secretary Gorbachev is for real. I think *perestroika* is something near and dear to his heart and has been for 6 years, in which he is trying to restructure the Soviet economy because the Soviet economy has failed.

And there isn't any question about that; so that we have a window of opportunity, I believe, to try to have an influence on him and how he tries to bring his economy into a market economy that is one that we shouldn't miss.

And I agree with you that if Gorbachev fails, that what we get next time around, I don't know what it might be. But I think that we should take advantage of this moment to see if we can't work with this group of people who are a totally new kind of cat, if that's the way you want to put it.

I was so impressed in our negotiations with the fact that they were willing to criticize each other publicly. I've never seen that in my dealing with the Soviets. They were very forthcoming.

I think that if we can help this, which, again, gets back to the human rights, if they start to be open in their society and talk about these kind of things, that we are achieving what we are trying to achieve.

Representative PORTER. So that you are willing to work with the Soviets on their concerns on trade with the West in credits, so long as they're more forthcoming on our concerns on human rights?

And you believe that if we fail to be forthcoming on their concerns, we may go back to the hard line where we won't achieve anything?

Secretary VERITY. Congressman, I think we're making tremendous progress, the fact that we have an arms control agreement and the start of another one, the fact that the Soviets have pulled out of Afghanistan.

Representative KEMP. Not yet, Mr. Secretary.

Secretary VERITY. They have indicated that they will. It would seem to me we should be delighted, Congressman, that they said they're going to pull out of Afghanistan.

These are all improvements. I told them very clearly when we were there that trade would follow the improvements, not lead

them; so that, until we do have arms control, until we do have less regional issues, until we do have a better example and progress on human rights and emigration, there will not be trade. Trade will follow. Trade will not drive it.

And I've been trying to make that clear to your Commission today.

Representative PORTER. What kind of mechanisms or procedures do you have within the Department of Commerce to take into account American values other than economic values; in other words, human rights?

Do you have something institutionalized or structured within the Department to bring these things forward?

Secretary VERITY. Well, I think we have the same kind of concerns that you do. I think I was more outspoken on human rights with the Soviet leadership than anyone has ever been.

Representative PORTER. Yes, sir, you were, and we certainly applaud you for doing that and are very gratified that you did that. But I was talking about what you had in the Department.

Is there anything there that is structured to look at things other than simply the economics of it?

Secretary VERITY. Well, Frank Vargo and Louie Laun, who are here today, have charge of that part of international trade. And I think that they, like everyone, looks at all aspects of a country that we're trading with.

And so, I don't know whether they want to speak up on this, but there isn't any question in my mind that, as we look at the full culture of the Soviet Union and what we'd like to see done in order for them to become a good trading partner, we do discuss all these issues that you're interested in.

Representative PORTER. Mr. Chairman?

Chairman HOYER. One more? No more. Thank you, Mr. Secretary.

Thank you, Congressman Porter.

Mr. Secretary, we could go on, literally, for 2 or 3 hours discussing this and we're going to pursue it. But for now, let me just add that we're very pleased, again, that your Department and the President have now appointed somebody to sit on our Commission.

We believe that this issue of East-West trade is going to be heightened and there is a need to address the difficult questions surrounding our own interests, both domestically and internationally, as it relates to what we want to do on trade.

We appreciate your testifying and your staying with us long enough to answer the questions. If you will, Mr. Secretary, I would like to submit some additional questions that, perhaps, you could answer.

Secretary VERITY. We'd be happy to answer any questions.

Chairman HOYER. Thank you very much, Mr. Secretary. We appreciate it.

Secretary VERITY. Enjoyed being with you.

Chairman HOYER. Next, I'm going to call a panel of four very distinguished persons. I appreciate their being with us and apologize for having them wait so long.

Mr. Richard Perle, who served as Assistant Secretary of Defense for International Security Policy from 1981 to 1987 and served as

the chairperson of a number of U.S. Government inter-agency groups, including those concerning arms control. As I mentioned earlier, Mr. Perle was the representative of the Defense Department on the Commission.

Next, Dr. Paula Stern. Dr. Paula Stern is senior associate at the Carnegie Endowment for International Peace. She served as Commissioner of the U.S. International Trade Commission from October 1978 to January 1987 and was chairperson of the ITC from June 1984 to June 1986.

Roger Robinson, president of R.W.R., Inc., a consulting firm advancing, "national interest," transactions and projects, internationally emphasizing areas of defense, communications, and energy. Prior to that, he was the senior director for International Economic Affairs at the National Security Council from April 1982 until September 1985.

Last, but certainly not least, Michael Bonsignore, currently president of Honeywell International, responsible for the company's activities outside of the United States. Honeywell has an extensive distribution network in 90 countries and raises one-quarter of its revenues outside the United States.

This is a particularly interesting panel. I'm pleased that we have so many of our members still here. I am going to start by recognizing Secretary Perle.

PANEL STATEMENTS OF RICHARD PERLE, PAULA STERN, ROGER ROBINSON AND MICHAEL BONSIGNORE

Secretary PERLE. Thank you very much, Mr. Chairman and members of the Commission. I should like to begin by thanking you for your consideration in asking me to testify today.

The issue of the relationship between trade, human rights, and, certainly, in the Helsinki context, national security, has long been of interest to me. It is an interest that developed out of nearly 11 years on the staff of the late Scoop Jackson, a man who cared deeply about human rights and national security and who believed that the United States had an obligation to do whatever it could to foster both.

On at least one aspect of the relationship between trade and human rights, our law is clear: We will not grant such trade concessions as most-favored-nation treatment and access to U.S. Government credits to nonmarket economy countries that deny their citizens the right and the opportunity to emigrate. This link is enshrined in the Jackson-Vanik amendment, about which much has been said today.

I was delighted to learn that Secretary of Commerce Verity used the occasion of his recent visit to Moscow to make it plain to the Soviet leaders that they can expect no departure from the provisions of Jackson-Vanik, that it will, in his words, "stay on the books."

He might have taken time to read Jackson-Vanik, in which case he could have given you a clearer answer to the question of what is entailed in that legislation. It does not apply only to Jewish emigration.

It applies to emigration in general. And it requires that countries offer for their citizens the right and the opportunity to emigrate. There are no specific numbers mentioned in the legislation.

This policy is, of course, that of the President and one to which he has long been deeply committed, together with all who have been nominated to run for the Presidency since the amendment was first proposed in 1972.

I hope and I trust that what was true in 1972 and 1976, 1980, and 1984 will also be true in 1988 and we will see the candidates of both parties rededicate themselves to the proposition that if goods are to flow freely from East to West, people must be allowed to do so also.

It is sometimes argued—and I think I caught a hint of this in Secretary Verity's formulation about the 30 to 35 percent penalty that's entailed in not having access to MFN, that expanding trade between the United States and the Soviet Union entails no concessions to the Soviet Union and that extending most-favored-nation treatment to the Soviet Union amounts to little more than the removal of discrimination against Soviet products entering the United States.

However, Mr. Chairman, the fact is that there can be no such thing as equal access to each other's market so long as the Soviets control their economy centrally.

When we open our market to Soviet products, they are given a full opportunity to compete against the products of our other trading partners as well as those manufactured here.

I don't know whether those small trucks will end up coming into the American market, but I imagine that there are people in Detroit who would not be delighted to see that happen, particularly at this moment.

But no U.S. Government agency controls potential buyers of Soviet goods. But when the formality of most-favored-nation status is extended by the Soviet Union to the United States, the result is quite different. A central government authority could, if it wished, vitiate the benefits of a nominal market access by instructing the purchasing entities under its control.

It is for this reason that MFN is not genuinely reciprocal, but represents a major Soviet concession—a major American concession to the Soviet Union, if and when it is extended.

The same is true, of course, with respect to access to credits. It doesn't take a banker to figure out in which direction credit is likely to flow if we and the Soviets agree that each is prepared to extend credit to the other.

Jackson-Vanik prohibits government credits from going to the Soviet Union. Removal of that restriction would be a major concession to the Soviets. So, in both these cases, we are talking about unrequited concessions, for which it seemed to the Congress in 1972–74 perfectly reasonable to ask for something in return. And the thing that was chosen was an improvement to the emigration policies of the Soviet Union.

Mr. Chairman, it is important to note that Jackson-Vanik was adopted with a view to easing these restrictions if the Soviets would ease their restrictions on emigration. This, they can do by

issuing exit permits to those who request them; not to some fraction, but to all of those who request them.

Toward this end, there is a provision in the legislation for a Presidential waiver which can be exercised if the President has received assurances, and reported them to the Congress, that there will be a liberalization of Soviet emigration practices.

I found Secretary Verity a little vague on the circumstances under which the waiver might be issued. And if he would look at the legislation, he would see that it is quite precise on this matter.

The President must meet two conditions. He must receive assurances from the Soviet side, and he must convey those assurances to the Congress of the United States.

Now, it's not enough simply to observe what is going on and then declare that a waiver is in order. There has to be a negotiation and, for practical purposes, an agreement as to the future conduct of the Soviet emigration policies.

Any such waiver would have to be renewed annually on the perfectly sensible principle that we ought not to make permanent concessions in exchange for what might turn out to be temporary progress in human rights.

And I think we have learned over and over again, and Poland is one example, that when you make concessions in exchange for the release of prisoners, you shouldn't be astonished if the prisoners are back in jail sometime thereafter, but the concessions can't be recovered. And, for that reason, Jackson-Vanik is temporary as a means of forcing continuing liberalization.

Let me conclude with just a word or two about two closely related issues. One is the sale of advanced technology to the Soviet Union and other countries of the Warsaw Pact. And the other is the extension of private credits from Western financial institutions to the Soviet bloc.

On the latter point, I won't say much because Roger Robinson, who's perhaps the nation's expert on this subject, is here with us today.

As I am sure members of the Commission know, the Soviet Union has relied for years on advanced Western technologies in the development and production of their major military programs.

We have one secret data that would still be secret were it not for the remarkable courage of a Soviet citizen who passed it to us that shows conclusively that, in the early 1980's, the Soviets relied on Western origin technologies in more than 5,000 military programs.

That is to say there were 5,000 active Soviet military programs for which the Soviets had targeted specific Western technologies, components, and the like. And they had a fully developed plan for acquiring this equipment.

We and our principal industrial allies, recognizing this, cooperate, though not nearly enough, in an agreed regime of restraint on exports of advanced technology to the Warsaw Pact.

It would be a tragic blunder, Mr. Chairman, to permit the desire for expanded trade to undermine the restraint, however imperfect, and it is imperfect. This last remaining Western advantage in a military balance that is increasingly adverse to the Western alliance is our superior technology.

Share that with the Soviets through foolish joint ventures or careless exports and we will see the military balance shift even faster, and much further, against us.

In the end, we will neither deepen—we will either deepen the risk to our own security or make it necessary to spend vast sums to counter our own technologies. We may even do both.

The recent Toshiba/Kongsberg case has illustrated how costly it is when technology that has profound military consequences falls into Soviet hands. We ought to expand trade in areas that will improve the lot of the Soviet consumer, but not the accuracy of Soviet missiles or the effectiveness of Soviet submarines.

And, finally, we should regard with concern, and at the very least with attention, the extent to which the Soviet Union is now raising Western capital, vital hard currency, through untied loans from Western financial institutions.

In 1986, nearly $2 billion per month was lent by Western lending institutions, especially those in Germany and Japan, to the Soviet Union and the Warsaw Pact.

None of these funds were tied to exports; none could be regarded as export credits. Our allies, who seem never to find the money to share the burdens of Western defense fairly, somehow have an abundance of ready cash when Moscow needs money.

And today's Washington Post reports a $2.1 billion loan to the Soviet Union from a consortium of West German banks led by the Deutsche Bank. That is a bank that is not invulnerable to influence from the West German Government.

This loan is untied, as far as we know, available to underwrite the Soviet defense budget, which presently claims upwards of 20 percent of the Soviet GNP, should they choose to use it in that way.

Or, it might be used to subsidize Cuba. Or Cubans in Angola. Or Vietnamese in Cambodia. Or worldwide intelligence operations. It would be up to the Soviet Union to decide how to use those untied credits.

The terms of the loan are believed to be favorable, bordering on concessionary. And the Secretary of Commerce didn't know what those terms are because they've been kept confidential. And one imagines they've been kept confidential because they would turn most Western borrowers green with envy.

And it comes at a time when the Germans, who are spending barely one-half as much as we are on defense on a per capita basis, claim that there is no cash available to even up the burdenance of alliance defenses.

This seems, to me, sheer folly. Those who believe that Soviet economic problems offer some hope that they will moderate their international behavior for economic motives should dwell on the implications of the Germans and Japanese rushing in to free them from the necessity to choose.

If the West showers hard currency on the men in the Kremlin, they may find a way to have their military budget and economic development, too. We may have yet to see—we have yet to see any domination of Soviet military spending.

Gorbachev has continued the Soviet military buildup that is now entering its third full decade; and he is doing it with support from Western banks.

Mr. Chairman, there can be no more noble purpose than enlarging the sphere of human freedom.

This Commission has labored long and hard over many years to turn the promise of the Helsinki Final Act into reality.

You have the gratitude of all of us who enjoy the great gift of individual liberty and hope to see it shared by those to whom it has been denied.

Chairman HOYER. Thank you for your statement, Mr. Perle.

I'd like to now recognize Dr. Paula Stern. Doctor?

Dr. STERN. Thank you, Mr. Chairman, members of this Commission. I want to thank you for giving me the opportunity to testify before this hearing on United States-Soviet trade, economic leverage, and human rights compliance in the context of the upcoming summit in Moscow.

It seems that whenever United States-Soviet political relations begin to warm, Washington officials get busy developing scenarios for removing barriers to trade with the Soviet Union.

The most prominent example of this phenomenon occurred in the era of détente in the early 1970's, culminating in the trade agreement signed at the May 1972 summit in Moscow between Richard Nixon and Leonid Brezhnev. That, of course, was "Détente 1."

This impulse last took hold at the time of the signing and consideration of ratification of SALT II back in 1979. You may recall then, that was when emigration figures and United States-Soviet trade figures were both at their height. But no one dared use the word "détente" in those times.

But, now, on the eve of the May 1988 summit between President Ronald Reagan and General Secretary Mikhail Gorbachev, comes another thaw and another shake of the trade thermometer to take the temperature of our relationship. And that, I suppose, is what we call "Détente 2."

Now, the intriguing question is whether Gorbachev's need to buy time at home by increasing the supply of food and consumer goods to its citizens in order to facilitate *perestroika* provides a promising new target for political opportunity for the United States.

While past attempts by the United States to wield economic leverage have generally been disappointing, a review of historical patterns and benchmarks can guide policymakers around future pitfalls.

A brief historical scan highlights how most-favored-nation tariff treatment, financial credits, export licenses, debt resettlement, and grain sales have been used as instruments of trade politics. I refer you to my written testimony, which details the history of these attempted uses of these tools of leverage.

But I'm here today to tell you that, while trade is a handmaiden of politics, it's a weak one, and it works best, when it works at all, when it's a carrot, not a stick.

Our leverage is limited first and foremost by the economic constraints on United States-Soviet trade itself. Trade matters less to the Soviet Union, which tends to be autarchic, than it does to the

United States, which finds itself increasingly economically interdependent.

Trade between the two nations is small, unbalanced, and composed mainly of raw materials, particularly grain. In effect, the Soviets can and do turn off the spigot anytime, even in the face of apparent need for Western goods and technology.

The United States is further constrained by domestic political groups, particularly farmers. We've seen this often when it came to the case of grain.

And, moreover, again, as the grain embargo post-Afghanistan suggests, it's difficult to get a united political position in the West when sanctions are attempted.

While United States-Soviet trade has grown substantially since the sixties, from less than $250 million back in 1971 to close to $2 billion in 1987, the trade has followed no steady course.

Because politics play such an important part in shaping the trade pattern between the two superpowers, the bilateral trade patterns in the seventies and eighties has been a matter of two steps forward and three steps back.

This limited basis for trade obviously limits the opportunities for leverage. It's just common sense. The Soviet Union, moreover, has avoided developing a relationship in which it becomes economically dependent on another powerful country.

And when the U.S.S.R. has entered Western markets, it has stayed for only short periods of time, often unbeknownst to the diplomatic community. And this, of course, was most shockingly apparent back during the great grain purchases of 1972 when those purchases were made completely unknown to Henry Kissinger who at the time was trying to exercise linkage.

Great irony there. And it's an outstanding example of how the Soviets do come in quickly when they're needy and we don't always know and are not able to capitalize on it. Trade with the United States mostly occurs at the Soviet's bidding. And, again, I refer you to my longer statement for numbers of examples of that occurring.

Some might conclude from all of this that the principal lesson learned from past efforts to tie political objectives to economic concessions, such as the Jackson amendment, is that economic leverage will never work.

However, even in the case of the Jackson amendment, Soviet leaders appeared to adjust their behavior, first, in response to Kissinger and Nixon, who gave or promised concessions on a number of matters before Jackson even introduced his amendment on trade, and then, later, the Soviets seemed to adjust their behavior to try to avert the Jackson amendment while it was pending but not yet approved in Congress.

Now, the success of a given policy of altering Soviet behavior depends largely on the objective of the exercise. The manner in which demands are couched, I think, is also important. If demands are presented belligerently and highly advertised, chances of successfully gaining concessions from a great power like the U.S.S.R. are less.

It may be true also that a policy of incentives, a carrot, carry less risk and greater chance of success than a policy of denial, a stick.

So, for the reasons described above, the United States may influence the Soviet Union, but, ultimately, the Soviets control the tap on emigration and on other matters of human rights.

Taking emigration figures for Soviet Jews as an indicator of human rights compliance, for example, it's clear that the Soviets control the timing and the numbers according to their own domestic decisionmaking.

When the Soviets are trying to court Western public opinion for tactical reasons—for example, when ratification of an arms control agreement is pending or access to Western financing or technology is desired by them—then the number of emigrants rises.

The number of Soviet emigrants reached the rate of 32,000 a year in 1972, before the Jackson amendment was even introduced. It rose marginally to an annual rate of 35,000 in 1973, when the amendment was pending.

It dropped in 1974 to 20,000, again, while the amendment was pending. And then it dropped further when the amendment was passed in 1974. In January 1975, the amendment was included in the trade bill signed by President Ford.

So there is a closer correlation, I believe, between the Soviets' desire to court Western public opinion, coincident with their desire for trade with the West, on the one hand, and the numbers of emigrants than there is between either the introduction or the pendency or the passage of the Jackson amendment and higher numbers of emigrants.

It's the Soviets who know what they want, come into the market, and will play on Western public opinion. And the emigrant figures more closely correlated with that than with the actual pendency and passage of the Jackson amendment.

Nevertheless, the United States, I think, must be very clear what the standards or criteria of desirable behavior are so that when the Soviets do desire to court Western public opinion, it will be clear to the Soviet leadership that human rights compliance, including freedom to emigrate, is a priority.

Insisting on human rights compliance as a part of the fabric of United States-Soviet relations doesn't stand in the way of trade between the superpowers. Human rights compliance, and the existence of the Jackson amendment on the law books, is not in and of itself a roadblock to commercial relations with the Soviets.

If you look at the tiny volumes, the erratic trends, the unbalanced basis of trade, it is clear that there are enough intrinsically economically based barriers to trade that will have to be dealt with before the Jackson amendment ever becomes a barrier.

Don't forget that the Jackson amendment provides a waiver, and if you might have forgotten, Richard Perle has reminded us again. That waiver provides that the President can provide Congress with assurances that Soviet policy allows freedom of emigration.

In short, it is far easier for the Soviet authorities to increase and sustain emigration than it is for them to increase and sustain exports profitably of Soviet manufactured goods in Western markets.

In sum, I would not exaggerate the utility of leverage, whether it is a carrot or stick. There is room for subtle gains here, but not crushing victories. Nor would I exaggerate the commercial potential of United States-Soviet trade.

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Both superpowers are losing clout relative to the other nations on the globe; the world is moving from a bipolar to a multipolar model. But it would be wrong to underestimate the need for the United States to be clear, consistent, and constant in its objectives when relating to the other great superpower of the world.

Finally, we need our allies to be part of a consistent position.

So, in closing, I'd like to make it clear that, while I have dwelled on emigration and the Jackson amendment as a metaphor for human rights compliance issues, I firmly believe the United States should not be interested in numbers alone, nor in a single ethnic group alone.

Open borders should be our concern, open for freedom of movement of individuals and for goods alike.

Thank you for your attention.

Chairman HOYER. Thank you, Dr. Stern. I next would like to call Mr. Roger Robinson, president of R.W.R., Inc.

Mr. ROBINSON. Thank you, Mr. Chairman. Prior to beginning my brief testimony, I would like to merely note that I have professionally participated in East-West trade and finance as a vice president of a major U.S. money center bank with responsibilities for the Soviet Union, Eastern Europe, and Yugoslavia for a 5-year period.

I welcome this opportunity to appear before the Helsinki Commission on the economic and financial dimensions of the Helsinki accords. The stature of Basket II of the accords, mandating the exploration of possibilities for expanded East-West economic activity, has risen in importance dramatically in the 1980's.

This development coincides with the Soviet bloc's growing need for major new infusions of Western capital, technology, equipment, management, and marketing skills to revitalize largely stagnant economies.

This need is intensified by the increased market competition confronting East bloc exports by those of the newly industrialized developing countries and the Third World.

Most experts agree that Eastern Europe faces a bleak economic future without radical economic reform, which, in turn, requires unprecedented political liberalization.

The much vaunted crisis of capitalism, predicted by the Communist world in the 1950's, has failed to materialize. Instead, today, we witness a crisis of Marxist Leninism, seen most vividly in the Communist less developed countries, but also evident in several Soviet bloc nations.

The view is often heard today that the most appropriate Western response to *perestroika* would be to step up Western assistance to the Soviet economy as a way of advancing Gorbachev's economic reform program.

Some of the same voices suggest that expanded Soviet integration into the global trading and financial systems would give Moscow "a greater stake in the system," and, hence, moderate its domestic and international behavior.

Rather than wait for a multiyear, concrete track record of improved performance on human rights, economic reform, and modified geopolitical behavior, we are urged by Moscow and many in the West to take Gorbachev at his word that this is, indeed, a new era in East-West relations that will permanently relax tensions.

We heard the same kind of pronouncements from General Jaruzelski just prior to the most recent crackdown on Solidarity.

Despite some progress in the area of human rights and the selective release of dissidents, certain Soviet actions have undermined confidence in this optimistic message concerning the "mutual benefit" of sharply expanded East-West trade and finance.

One is the enormous increase in Soviet military investment and weapons procurements in the 1970's and 1980's, which has enabled Moscow to gain clear-cut superiority in conventional forces in the European theatre.

A considerable part of the Warsaw Pact's military prowess, as Richard Perle has mentioned, is attributable to the acquisition of Western technology. In addition to an unrelenting military buildup, the Soviets have amply demonstrated their ability to project power in the Third World, largely by military means.

It is ironic that some relaxation of tension in Europe has been accompanied by a rise in low intensity conflicts in the developing world. Europe, arguably, is more at peace, but the LCD's have become the primary victims of Soviet-sponsored aggression.

Another regrettable development has been the obstinacy with which the Soviet bloc regimes have resisted their broader human rights obligations under Basket III.

Aside from the Polish experiment in 1979 through 1981, which was abruptly terminated, not a single East European country has taken its Basket III obligations seriously.

The question, therefore, seems to be—should the West quickly intensify its economic and financial activities with the East in the absence of sustained and material progress in the area of human rights and military security?

Moreover, does it make good policy sense to focus our limited economic and financial resources on assisting the U.S.S.R. and Eastern Europe when so many of the high debt democracies in Latin America and elsewhere are also in need of urgent attention and where the opportunities for future Western exports and employment are immeasurably greater?

I believe that a policy of unfettered trade and finance with Soviet bloc countries decoupled from the balanced objectives of the Helsinki accords would not only contradict our basic values, it could also set back, rather than advance, the cause of genuine economic reform.

The centrally controlled economies of the East bloc have tended to attract greater Western trade and financial flows as a substitute for reforms rather than a stimulus.

Soviet bloc leaders traditionally have found it easier to import technologies and critically needed goods than to release the controls on their economies which inhibit innovation and entrepreneurship.

In the past, this preference for trade and borrowing from the West in lieu of reforms on the part of East European countries helped produce the debt crisis which still grips much of the region.

In the case of the U.S.S.R., the reforms are impeded by the unyielding Soviet commitment to a militarized economy and the perceived need to underwrite a global empire.

This helps explain why economic reforms are making far greater headway in the People's Republic of China than in the Soviet Union. China has dramatically reduced military outlays and has no expensive foreign empire draining scarce resources.

Given these realities, it is evident that a politically influenced Western bailout of the Soviet bloc in the form of government-guaranteed untied loans of the kind recently made by West Germany to Hungary, government-sponsored joint ventures in the energy sector, subsidized trade, and substantially expanded access to high technology is not appropriate in the absence of systemic economic reforms and broad-based human rights liberalization.

(This statement does not imply any effort to impede the normal market-oriented expansion of nonstrategic trade and finance.)

An economic rescue of the Soviet bloc of the type described would merely perpetuate the inefficiencies that are robbing Eastern Europe of its economic future and permit the U.S.S.R. to continue its military buildup and global adventurism at the expense of its civilian economy.

The written testimony which I have submitted for the record of these hearings on the subject of economic and financial burden-sharing seeks to outline briefly proposed alliance policy prescriptions in the field of economic and financial security, including recommended Western responses to the current and projected Soviet economic agenda toward the West.

Generally, I recommend a cautious and prudent approach to increasing economic and financial relations which, hopefully, reflects the middle ground between undue trade restrictions and unfettered Soviet bloc access to valuable Western resources.

I believe the proposed policies and reaffirmation of existing policies would also advance prospects for arms control as the Soviets would have a greater incentive to make the kinds of positive trade-offs between their military and civilian economies that we are hopeful of seeing in the context of *perestroika.*

Finally, the lack of Western public support for increased defense spending to modernize our conventional and nuclear forces and maintain an effective global basing structure argue strongly for coordinated economic and financial security policies becoming the next major defense burden-sharing obligation for the alliance.

Such policies would not only accelerate movement towards arms control and genuine East bloc economic reform, but could, over time, result in multibillion dollar defense-related savings annually for the American people.

Thank you, Mr. Chairman. And I would appreciate, if I may, having this oral testimony together with a 1-page statement I have prepared on the subject of the $2.1 billion West German credit line just made available to the Soviet Union be included in the record of this hearing, with your permission.

Chairman HOYER. Without objection, all of the prepared statements will be included in their entirety.

Next, I'd like to recognize Mr. Bonsignore—I'm not sure I have that right yet, but it's written about 3 times here as to how I'm supposed to say it—who, as I said earlier, is the president of Honeywell International.

We're very pleased to have you with us and we appreciate your batting cleanup for us.

Mr. BONSIGNORE. Thank you, sir. Well, Mr. Chairman and members of the Commission, it is a pleasure for me to be here today to contribute to this important topic and to tell you a little bit about Honeywell's past, present, and potential business experience in and with the U.S.S.R.

I've elected to abbreviate my oral comments somewhat in the interest of time, but my entire testimony is in written form and available.

As you know, on April 14, 1988, Honeywell entered into an industrial automation joint venture agreement with legal entities of the Ministry of Mineral Fertilizer Production of the U.S.S.R., subject now only to registration by the Ministry of Finance, which we anticipate will be completed by the end of June.

While that event became worth of note in today's environment, it should properly be considered in the broader context of Honeywell's international activities over an extended timescale and the truly global nature of the process control systems business.

And for the audience, I would like to generalize and say that "process control system" implies a supervisory controlled system which would monitor and manage a continuous, or batch, process for the production of things like fertilizer, gasoline, steel, plastics, any other type of petrochemical. That's what I mean by the "process control" business.

We believe that the formation of a joint venture at this time can significantly expand our potential market within the U.S.S.R. and that doing so is a consistent extension of Honeywell's strategy to aggressively expand our international business in key markets.

Looking at our commercial, that is, our nondefense business operations, and taking into account our sizable nonconsolidated Japanese affiliate, fully one-half of Honeywell's activities are outside the United States.

We utilize a broad range of approaches in the international arena, starting with 42 wholly-owned subsidiaries and ranging through joint ventures, representative offices, licensees, and 94 independent distributors.

Recent joint venture activities prior to the U.S.S.R. cover the political spectrum from South Korea and Saudi Arabia through India to Bulgaria.

Our participation in the Russian market is not a new idea. Honeywell has maintained a representative office in Moscow since 1974, admittedly, through peaks and valleys of the political and business environment.

More than 60 of the Fertilizer Ministry's production plants have Honeywell controls in place, some dating back to 1960, mostly installed by international construction companies.

The Moscow hotel where we stayed last month during the U.S.-U.S.S.R. Trade and Economic Council meeting is equipped with an integrated Honeywell building control system.

So you can see that our decision to participate in an industrial joint venture was a logical next step, given the business climate that is evident in the U.S.S.R. now.

Under the U.S.S.R. joint venture law as revised in the fall of 1987, each ministry was empowered to enter into such ventures utilizing its juridical entities and based upon the hard currency reserves available to it.

Within this environment and given that Honeywell has executed several other joint ventures involving the transfer of complex technology without majority ownership, negotiations proceeded more smoothly than most would have expected. In fact, our overall schedule laid out in June 1987 was met.

We maintained continuous communication with cognizant agencies and departments of the U.S. Government and scheduled many meetings with other elements of the Soviet Government.

Given the lack of direct business experience in our partners-to-be, meetings such as those with the Ministries of Finance and Foreign Affairs, the Government Insurance Company, and others were an important part of the education process for both of us.

We discovered that most of the key bureaucrats that we came in contact with were relatively young and had been in their places for a fairly short period of time.

It became clear that we were dealing with a different and new generation of government officials who were highly motivated to make change happen. As in any large organization, however, a decision for change at the top, even accompanied by a strong desire for change at the bottom, creates a very uncomfortable middle bureaucracy.

Even within our partner ministry, it was clear that there were certain people who were either not supportive of the changes around them or not prepared to believe in them yet. Its senior management, however, was consistently open to compromise, was continuously supportive, and displayed a problem-solving orientation.

Through this open relationship, we have certainly been warned of and, in some cases, have already begun to see, the lower level bureaucratic problems that our new joint enterprise will indeed face.

One issue currently being worked is the difficulty in dealing with city officials for the acquisition of appropriate space and facilities. We fully expect similar problems in areas such as communications and the mobility of our personnel.

These situations are not unique to the U.S.S.R., however, and we feel confident that, with periodic intercession by our partner ministry, such problems and delays can be overcome.

Although we have done our best to protect ourselves contractually, we obviously recognize that, in any venture, the choice and the power of the potential partner is perhaps the most important success factor.

In addition to the direct sale by Honeywell of a $2.2 million process control system upgrade for a major fertilizer plant in Novomoskovsk, our Soviet partner has committed to the new joint venture eight more such upgrades over the first 2 years of operation.

It is important to understand that the Ministry of Mineral Fertilizer is the world's largest exporter of fertilizer. As such, it is a net generator of hard currency for the U.S.S.R.

Its primary hard currency expenses consist of plant construction and upgrades, typically with Japanese and European plantmakers. It is this industrial priority in the U.S.S.R. that gives our joint venture life and substance.

We will be exporting process control equipment to the Soviets and we will be paid in hard currency for those exports. Soviet value-added, however, will eventually represent approximately one-half of the total system cost because of the systems design and configuration, application software development, installation and maintenance activities which go on in-country.

This ratio of local value-added versus imports, creates two separate but complementary mutual benefits for the partners.

First, the decreased need for hard currency per system enables the modernization program to proceed at a faster pace with the importation of more systems hardware.

Second, the improved quality control of the newer systems increases the actual output from existing facilities, enabling additional fertilizer export, which, once again, generates hard currency.

As you know, it is an important goal of the Eastern bloc to achieve free market economies by the 1990's and, ultimately, full convertibility of their currencies.

We feel that our joint venture can proceed successfully on its own merits in the interim, however, because of the functional advantages that I have just mentioned. Hopefully, the ultimate goal of full and free trade can also be realized one day.

The benefits to Honeywell and the United States, however, are by no means limited to fertilizer production or, for that matter, to the broader process control arena.

Even while our talks were going on in Moscow, there was a completely separate automotive trade show in process, and Honeywell was able to execute both direct orders and licenses in support of the Soviet auto industry with clear indications from the U.S.S.R. buyers that our investment in their country was an influencing factor.

There is strong Japanese and European competition evaluating the Soviet market in response to the favorable business climate of late. Honeywell was fortunate to draw on our experience in the U.S.S.R. to gain approval for one of the first joint ventures in our line of business.

Finally, we and some other American companies have taken some relatively risky steps in response to inter-governmental actions that could potentially improve and solidify the opportunities for trade between the United States and the U.S.S.R.

Secretary Verity's presence in Moscow during the recent U.S.-U.S.S.R. Trade and Economic Council meeting was certainly welcomed. Everyone of the Fertilizer Ministry officials that I spoke with that week hoped that our joint venture would provide a basis for better understanding between our two nations.

Unfortunately, however, we have seen these expectations before, only to have them evaporate as political differences soured the trade and economic climate and branded both of us as unreliable trading partners.

We are truly encouraged by the environment we have encountered in the U.S.S.R. recently and the willingness of the Soviets to

compromise and structure mutually beneficial and balanced business deals.

We feel it is in the interest of the United States to move toward bilateral agreements with the U.S.S.R. that reinforce trade as a vehicle of peace and protect the partners from after-the-fact interference.

There is tremendous trading opportunity between the two nations, but only a concerted effort to rebuild our mutual trust can realize this full potential.

So we'd like to thank you for your attention, and we hope we've been of some assistance in relating our experience to those of the broader issues at hand here. Thank you.

Chairman HOYER. Thank you very much. Let me start with a question for you, Mr. Bonsignore. With respect to all the other witnesses, uniquely, you want to make a profit and you want to do business with markets that you find to be successful to deal with; correct, I presume, I hope?

Mr. BONSIGNORE. Yes, sir.

Chairman HOYER. Now, what role, if any, does the human rights performance, which we have discussed a lot today, play in determinations that Honeywell makes, for instance, as a representative successful company in the West and, more particularly, in the United States?

Mr. BONSIGNORE. Well, let me try and answer the question from two points of view. The first is whatever we have done in the U.S.S.R. to date and certainly whatever we will plan to do in the future will be in compliance with the U.S. law in place at that particular point in time.

Honeywell's international business around the world simply cannot put itself in an untenable position of risk relative to some inordinate action which might be taken in a market like the U.S.S.R. or anywhere else. So the compliance with U.S. law is extremely important.

Beyond that, the corporate position is a little less specific in the sense that I think every time we have one of these business dealings outside the United States, we have to take it in consideration relative to the environment that we are dealing with in real time.

And there was some debate in our company relative to the position of the Soviet presence in Afghanistan and, as Secretary Verity mentioned earlier, the progress, perhaps not fast enough from everybody's point of view, but the progress in getting the Soviets out of Afghanistan; the issue of emigration in the broad context that it was discussed today.

There's no question in our minds that, as this whole scenario moves forward, we could be sadly disappointed by the whole thing. We've built adequate escape clauses into our joint venture for lots of reasons, not the least of which is the political environment between the two countries and the impact of that political environment on Honeywell's ability to do its business around the world.

So we've tried to take a look at it from those two points of view, and we recognize that nothing is guaranteed. But, because we are an international leader in this kind of business and we are competing against other international entities in Europe, Japan, and the United States, we've taken a wait-and-see attitude and proceed as

we go, recognizing, as I said in my testimony, we've been disappointed before.

Chairman HOYER. Thank you. Congressman Kemp has to leave. I want to follow up, but let me——

Representative KEMP. Thank you, Mr. Chairman.

Chairman HOYER [continuing]. Let me recognize Congressman Kemp.

Representative KEMP. I have to leave. I have a meeting in my office. I apologize to you, Mr. Chairman, and thank you for your graciousness in allowing me to ask a couple of questions.

Before I do, let me say to you, Mr. Bonsignore, they're not just "political differences" between the United States and the Soviet Union, you just stated. I would not move to lecture you on how to testify before the U.S. Congress, but, just as a piece of advice to a fellow believer in free enterprise and——

Chairman HOYER. Like all of us.

Representative KEMP [continuing]. International business competition, I'd come before this Commission and identify a little bit more closely with the purpose of this hearing.

To label the differences between the United States of America and the Soviet Union as "political differences," you might find a better way of expressing it, with all due respect.

The other point I wanted to make is that—again, apologizing—I'm not trying to embarrass you at all—do you really believe the East European countries and the Soviet Union have as a political and economic goal a free market economy by any time in your lifetime or mine?

There is empirical evidence available today that socialism doesn't work. Everywhere that market-oriented economies are being tried, they aren't working from Asia to Africa.

If they haven't tried it by now, do you think there might be more than just a political difference involved in the Soviet Union's adherence to a failed, outmoded, bureaucratic, totalitarian economic system that is defunct intellectually? It is defunct politically. It is defunct economically. And I just would hope, sir, as you spread the word about Honeywell and your business around the world, that you might give some greater thought, if you don't mind me saying so, to the fact that Soviet Union is a Third World economy. It can't compete. It needs access to Western markets, credit, and technology.

I've got to say, sir, I was disappointed in your testimony. For the record, since you found out from the Minister of Fertilizer that they wish to have better relations with the West—Who is the Minister of Fertilizer?

Mr. BONSIGNORE. Olshansky, sir.

Representative KEMP. Olshansky. I want to remember that name. Minister of Fertilizer Olshansky. Did you really believe, as a businessman from the West, that you're dealing with a country that wants a free market economy by the 1990's?

Mr. BONSIGNORE. Well, Mr. Congressman, we're trying to take a long view on this, as we do in all of these market formation issues. As I said earlier, first of all, I was asked to come here and testify about what Honeywell's participation in the U.S.-U.S.S.R. joint venture environment was, not to comment on the merits or demer-

its of some of the other issues that have been discussed here, but to give you in real time what is happening between our company and our Soviet partner as a result of the change in the law and the change in the environment.

I also tried to mention earlier that this is very much a trial and error, go-as-we-can environment.

Representative KEMP. Right.

Mr. BONSIGNORE. And I would hope, perhaps, that we're not unduly optimistic, that we try and take the high road in these business arrangements in every case; not only in the U.S.S.R., but in all of the other countries where we're trying to do business.

Representative KEMP. Well, you did make a political comment. You said they want a free market economy by the 1990's. I just wondered. Do you really believe that? What evidence is there? Why would you make that statement?

Mr. BONSIGNORE. Well, I think the issue here is. Will the relationship between the United States and U.S.S.R. in these joint ventures, which, I think, to a large degree, will be limited by the convertibility of the currency and many of the other issues that have constrained our trade to this point in time for reasons other than purely political; I think there has to be some recognitior. by the Soviet Union for the importance of the free trade issue, for the convertibility of the Soviet currency in the long term.

Representative KEMP. Right.

Mr. BONSIGNORE. I agree with you that they are a Third World country, and I also agree that they have reached a point, in my belief and their own thinking, that something has to change.

And there has to be some progress on some of these issues where there's been little or no demonstrated progress in the past.

Representative KEMP. Well, I'm glad you're here, really. And I don't mean to, as I said, try to embarrass you. I just would hope that a businessman doing business in the Soviet Union and a Western—a believer in Western-style democratic capitalism—thinks a little bit more of his own system, as I know you do—I know you must; than just to suggest there are political differences between the two sides.

It smacks of something, kind of a moral equivocating that Jeane Kirkpatrick denounced so recently, and I don't think you want to give that impression.

I want to applaud, Mr. Chairman, the panel, and thank, particularly, you, Dr. Stern, and you, Richard and Roger Robinson, for focusing on the linkage between trade and human rights. Whether we totally agree or not, I think your testimony on the MFN is extremely important.

I particularly was pleased to hear Richard and Roger talk so emphatically about the untied loan situation because I think it's going to turn into a national scandal.

Mr. Chairman, I predict that—absent fundamental change in the behavior of the Soviet Union—untied loans being made by Western Banks to the Soviet Union at interest rates more favorable to that country than to countries in Latin America, this will be a national scandal. I'd like to point out that these very same Latin American countries, which are being squeezed by the New York City banks,

are more important to us in the long run than this trade with the Soviet Union.

I wanted to just urge, Mr. Chairman, greater attention be focused on this issue. You, sir, have been one of the few willing to give attention to this issue. And it's going to be a scandal. It's going to be a scandal.

And Robinson and Perle are to be applauded for bringing this to the attention of the Congress. I think something has to be done to alert the American people about what we're doing to our allies in Latin America while we're rushing into Détente 2, as Dr. Stern pointed out, without getting the type of behavioral modification.

You don't have to be a "Skinnerian" to believe that there's got to be a change in the Soviet behavior before we give them this type of treatment.

So thank you for your courageous testimony as well as perceptions of this issue. Thank you.

Chairman HOYER. Thank you. My fellow "Skinnerians"——

Representative KEMP. "B.F. Skinner."

Chairman HOYER. Thank you.

Representative KEMP. Behavioral modification.

Chairman HOYER. All right. Appreciate the education. Let me go back, if I can, because you represent, really, I think, Mr. Bonsignore, an important element of what we're talking about.

I'd be very interested. You were in Moscow with a group of 400 or 500 business leaders?

Mr. BONSIGNORE. Yes, sir.

Chairman HOYER. How much discussion was there of the question of human rights as it relates to the Congress and its policies, as it relates to the favorable business opportunities and climate?

In other words, what I'm saying is, we tend to talk a lot about that. Obviously, we're dealing with different constituencies. You're dealing with stockholders who want profit. I have a sense that if we can merge the two more effectively, we will be more effective in making our case to the Soviets for the same reason because they're right now interested in profitmaking.

My questions is first, Was there discussion about that? and; How do you think we can do it?

Mr. BONSIGNORE. Well, first of all, in my own personal discussions with my Soviet counterparts, the subject of the Honeywell principles came up from time-to-time.

We have seven operating principles that we adhere to in our company, and one of those talks about no discrimination for race or color in employment opportunity, and things like that.

Simply as a modus operandi within our company, we are dealing in a lot of places around the world with a lot of different ethnic groups, our success as a corporation depends on our ability to demonstrate equal opportunity throughout our organization.

But beyond that point, I would say that the discussion was not preoccupied with the issue of human rights. To some degree, I think, businessmen, and I think I speak for the others, find ourselves in the middle of a very formative stage now in the Soviet Union where the lip service is very encouraging.

There is a great deal of skepticism built into the model from years and years of lack of mutual trust. There is the pressure

around the world to acknowledge that our marketplace has become very global in nature.

And then to ignore a legitimate opportunity to open better channels of trade between the United States and the U.S.S.R., as far as the American business community is concerned, would be a mistake in principle. We are, at the same time, influenced by a very dynamic set of factors that have a bearing on what our future will be; the progress on trade negotiations, the progress on arms limitation, the progress on the emigration issue.

And so I think we have tried to make a decision in the midst of this very dynamic environment to take a position to form a joint venture within the U.S. law and within the Soviet law and to use this as an opportunity for us to influence our Soviet partners with the way we do business, what our value system is, why we walk away from business when there are unethical practices involved.

We can transmit a little bit of conservative, Minnesota values to our Soviet counterparts and within their line of thinking.

But, again, I must say, as I've said before, I do this with some reservation, recognizing that the risk is very high relative to a more predictable environment. So the issue is, do we ignore it or do we try and become a part of the process by moving forward with some legitimate business vehicle to build on for the future?

Chairman HOYER. Let me ask one additional question before I recognize Congressman Porter. With respect to the three of you, I'd like to hear your comments on that facet of the problem because, the way I see it, those of you who have been involved in the public sector see it from that perspective, the political specter that really concentrates on the political facet of the relationship, the translation of our value system, the accomplishment of Helsinki objectives, as opposed to what Honeywell clearly ought to look at.

And maybe what they ought to look at is how to get a return to their stockholders on their investment. We're all for the free market, and that's what the free market is all about, them being able to make that free election.

I'd like to hear, perhaps, your perspectives on that issue. I think it's particularly relevant. As Secretary Verity and 400 major business leaders in our country and, obviously, major business leaders in Europe and in the Far East are now interrelating, making untied loans, entering into joint ventures and opening up their technology to others, how do you see the relationship between our public agenda and that private sector agenda? And how can we make it closer?

Secretary PERLE. Well, if I might take a crack at that, Mr. Chairman, it does seem to me that, ultimately, it is the responsibility of government to try to fashion whatever leverage attaches to trade and commerce into an instrument for the realization of national objectives.

And it is unrealistic to expect industry to assume those burdens. They do have an obligation to their shareholders. And, as a practical matter, they will not replace the Government in making the kinds of decisions and taking the kinds of actions that might have some influence on these matters. So I think it's unfair and unreasonable to expect that.

At the same time, we shouldn't kid ourselves. When industry decides to make an investment in a country like the Soviet Union, it easily becomes a lobby for the Soviet point of view downstream.

You can be sure that companies doing business in the Soviet Union, participants in joint ventures that have real interests at stake, will be unlikely to join in the call for disrupting business relations as a way of attempting to influence Soviet behavior if there should be some event in the future that would raise that issue.

They can be counted upon to oppose governmental action that would come at the expense of success in their commercial ventures.

Chairman HOYER. Dr. Stern or Mr. Robinson?

Dr. STERN. Having spent 9 years as a Commissioner and including 2 years as Chairwoman of the International Trade Commission, I see how America become increasingly internationalized economically and, thereby, politically increasingly interdependent. So my estimate of our ability to influence the Soviet Union regarding our notions of the appropriate human rights guarantees has been diminished.

The past decade has meant diminished leverage on the Soviets, and, as I've tried to point out in my written statement, influence has been only occasional.

Saying that, however, you raise then the question of what do you do with your allies? Allied cooperation has always been very, very important when we've tried to get a message across to the Soviet Union that is a consistent message about our human rights relations.

And it is even more important today. We have had periods when the allies were totally in line with the message we were trying to get across to the Soviet Union, most prominently during the Korean war, periods such as that.

Since then, we've had more difficulty. Of course, the height of our difficulties and differences was during the oil and gas pipeline period in the early eighties and during the Reagan administration.

So I would say that, while I think it's very important for us to have a consistent and clear line when all of our public and private officials are interacting with Soviet public officials about the importance of human rights, I think we have to understand that our influence is enhanced only if we have our allies also in line.

Richard Perle has raised this concern that an industry or a firm or a business that might build up a business relationship with the Soviet Union would ultimately become a lobby in the future when the time may come, when we would want to pull back on our trading relationship with the Soviet Union. I believe that history shows that when the American public is concerned about a human rights issue—and I think the Jackson amendment is a very prominent example of that—business really has not had that much influence over the ultimate outcome of the message that we send to the Soviet Union.

But I would say, just in conclusion, that this consistency is critically important. But I would, again, not exaggerate our influence as a government vis-a-vis the Soviet Union. I wouldn't exaggerate it, not only because of the allied problem which we've had over the years, but because of the increasing economic interdependence that we find characterizes many of our companies.

Honeywell International is a perfect example of that. My colleague's statement today indicated how much of Honeywell's activities in the U.S.S.R. involves its Japanese affiliate and how much of that is influenced by overseas actions and events.

So—when you look at your question—when you look at an American company, you really have to parse that and see really how American it really is now.

Chairman HOYER. Mr. Robinson?

Mr. ROBINSON. Yes, Mr. Chairman. I have some fundamental differences in view concerning the extent of Western leverage today, particularly when we look at this as an alliance, which is the only practical way to look at it. With that, I agree.

But let's look at the numbers, it seems to me, when assessing our ability to influence improved Soviet human rights performance with a carefully crafted public sector policy and close working relationship with the private sector.

The Soviet Union had in 1986, some $30 billion in total Soviet hard currency income. That's a little over one-quarter of General Motors' total sales for the same year.

Eighty to ninety percent of that amount was derived from exports of just four items: oil, gas, arms, and gold, attesting to the failure of the Soviets to successfully implement a diversified base of exportable manufactured goods.

They had to come to the credit markets due to those hard currency shortfalls, as Richard mentioned, to the tune of about $2 billion a month, $1.6 billion of which was untied cash; that is, no underlying trade transactions or projects.

The Soviets now have entered the international securities markets for the first time in history, seeking to recruit Western securities firms, pension funds, insurance companies, corporations, even individuals, as new, first-time lenders of untied funds to the Soviet Union.

And, yet, we in the West are taking these actions, which is all reflective of an ambitious Soviet economic agenda toward the West, without the kind of discipline and transparency that would be prudent not only from a national security and a commercial perspective, but also a human rights perspective.

I believe that the Government does have a unique role in the context of economic summitry, with the Toronto Economic Summit as a fine example upcoming, where it's incumbent on the U.S. President to persuade our allies to initiate the multilateral task of implementing greater discipline and transparency on financial flows, for example, and to impress on the private sector, in this case, the world banking community, that there are national security and even strategic implications in this untied lending practice.

And, indeed, we also want to avoid the kind of quick fix bailout of Soviet and Warsaw Pact economic problems prior to the kind of broad-based liberalization of human rights that are required under the Helsinki accords.

I think that the key word is leadership and that we have the institutional fora like economic summitry, like the OECD, like the Economic Committee of NATO, and Basket II of the Helsinki accords, which are mandated to do precisely this kind of work. We can stitch together more closely the public and private sectors of

alliance countries to not only advance our common security, but to do more to advance the cause of human rights and, in the process, get back to some good solid commercial banking practices as opposed to the kind of undisciplined cash lending that today is duplicating the exact kind of untied lending to sovereign borrowers that helped create a $1 trillion international debt crisis.

Chairman HOYER. Thank you.

Congressman Porter?

Representative PORTER. For Richard Perle. I agreed with so much of what you said I—this is somewhat off the subject, but if our allies, like West Germany, are granting loans to the Soviet Union that can be used for their own military purposes or any other domestic purpose without any ties whatsoever, what can the United States do to dissuade this kind of conduct that is really not in our national interest, nor in the interest of our allies?

Secretary PERLE. When dealing with friends and allies, there are limits, obviously, to the instruments at our disposal, but a good strong argument is of importance in these matters.

And I think we have a good strong argument, but someone's got to begin to make it. And, to the best of my knowledge, this is not an issue with which the Commerce Department has been seized.

And you heard Secretary Verity. He thinks it's a terrific idea, so he's not about to make the argument. It ought to come from the Department of State, but my guess is it won't originate there either.

At the end of the day, if it were the policy of the administration, of the President, and his principal advisers to discourage this sort of untied lending, it would have an effect. I don't think it's going to come to an abrupt halt, because there are different outlooks among some of our close allies and partners; the Germans, in particular.

But I think we could diminish it and we could make it very plain to our friends and allies that, if they have cash available for this purpose, we'd like to have some serious discussions about financing the NATO alliance because, when we attempt to talk about that, what we tend to hear is how the resources are simply not available. And that, obviously, is not the case.

Representative PORTER. Am I correct that there are restrictions on U.S. banks making loans of this type, not just to the Soviet Union, but to other foreign countries?

Could this happen in our own banking system?

Secretary PERLE. I believe it could, but Roger is the expert on that.

Representative PORTER. Oh, all right. Roger, what's your answer?

Mr. ROBINSON. The Johnson Debt Default Act of 1934 prohibits untied lending, as I understand it, to countries that are in default on obligations to the U.S. Government. The Soviet Union happens to be such a Government because of the czarist debt and, at least as I understand it, also Lend-Lease payments. Therefore, to make untied loans out of the U.S. banks, from their operations in this country is illegal.

Representative PORTER. I thought that there were some amendments to the—when we provided an increase in capital for the INF back in 1984, I think it was, didn't we put in some restrictive amendments on U.S. bank lending then?

Mr. ROBINSON. I'm not familiar with that particular issue, Mr. Porter. But I will say that there is a loophole, as I understand it, in the Johnson Debt Default Act, which has to do with the Soviets—whereby U.S. banks can lend those untied funds out of offshore branches and subsidiaries. And, as a consequence, the industry has moved in that direction, and that's where most of that kind of activity is coming from.

But, if I may go back to your earlier question as to how we could successfully and in a constructive way dissuade the banks of alliance countries away from untied loans and toward greater specific purpose, disciplined loans. I think the answer is the Toronto Economic Summit.

I think that the Congress has a constructive role it could play in urging that development. The administration often hears advice and counsel from Congress on these kinds of matters. Because it is the kind of thing that we have succeeded in doing on a number of other occasions, and I want to just cite a couple. We successfully eliminated subsidized terms on official credits to the Soviet Union in 1982.

We had made no such loans as a country at the time. And, yet, our allies were persuaded, albeit with difficulty, to discourage this practice, and we have an agreement in the OECD, Organization of Economic Cooperation and Development, in Paris to accomplish this, stemming from efforts in July 1982.

We got an agreement in 1986 to discourage our allies from making so-called "tied credits," but this time "tied" in the sense of the excessive use of grant money in development loans. As I understand it, our country had none, yet we succeeded in achieving an alliance accord, again, in the OECD with our allies.

We succeeded in limiting, in effect, Soviet gas deliveries to Western Europe. We weren't taking any Soviet gas. But we brought our allies into agreement, signed in the International Energy Agency in May 1983 under the OECD, which limits, as I said, Soviet gas supplies to Western Europe to those amounts already contracted by year-end of 1982, in favor of more secure Norwegian supplies and other secure Western suppliers.

So the fact is that there are three major precedents that I've just stated where our "share of the action," so to speak, was marginal to nonexistent. And, yet, with persistent diplomacy at the highest levels, we were able to succeed.

That's why the summit partners tasking the OECD, as we did in these other cases in the context of economic summitry, was the formula that led us to success in the past, and that's the one I would recommend for untied loans.

Representative PORTER. Mr. Chairman, I have one more question if I may.

Chairman HOYER. Congressman?

Representative PORTER. And this is, again, for Richard Perle. I'd like to go back to the question I asked Secretary Verity; and that is: If we assume that the Soviets under Mr. Gorbachev have been somewhat more forthcoming on some of the concerns that we have about U.S. security and U.S. values, what is the risk of our not being at all responsive to Mr. Gorbachev's needs and desires?

And could we risk falling back to a period where the hard liners in the Soviet Union who will give us nothing of what we seek from them—isn't that a real problem?

And should—what should we really do in terms of our relationship?

Secretary PERLE. Well, this strikes me as the most difficult and, at the same time, the most interesting of all of the questions in this area. I am persuaded, much like Secretary Verity, that Mikhail Gorbachev is attempting quite broad structural changes in the Soviet Union with a view to improving economic performance, which he recognizes to be bad and getting worse.

And I think he understands that the Soviet economy is slipping relative to the Western industrial world to the point where it may become a permanent second- or even third-class power, and he wants to change that.

I think he's got his work cut out for him because creating the sort of system in which performance is rewarded, which is bound to diminish the authority of the Communist Party where it is not performance, but position that is rewarded, that has never been successfully done in a Communist totalitarian state. And I have my doubts about whether he will succeed in his efforts to do so.

Thus far, we have not seen a significant change in Soviet external policies. They continue to invest in military power, much as they did before Gorbachev. They continue to underwrite the Cubans and the Vietnamese and others, much as they did before.

They are, we hope, in the process of withdrawing from Afghanistan, but I think that, like Gorbachev's economic reforms, represents a recognition that they have failed and were in a hopeless quagmire in Afghanistan rather than a gesture of moderation.

So I think we ought to keep looking for signs that external policy, as well as internal policy, are subject to change. When we see those signs, then I think we ought to respond to them. I don't take the view that we should be unresponsive.

But I think we want to be very careful about responding in a way that relieves the pressure to reform rather than encouraging pressure to reform. I've been struck over the years talking to people like Vladimir Bukovsky and Natan Scharansky, who all seem to hold the view that if the West offers improvident assistance to the Soviets, then the pressure for change will, in fact, be diminished.

They won't have to choose between the growth and development of their economy, on the one hand, and their military sector, on the other. They won't have to liberalize internally in order to encourage creativity and performance because it's vital to do that to improve their economic well-being.

Now, managing that process of rewarding positive developments in the Soviet Union is extraordinarily difficult to do.

But I would make only one further comment, which is that, if and when we find a basis for responding to what we think are positive Soviet developments, we should respond with temporary measures to temporary changes and not with permanent measures.

I would put in the latter category decisions like a decision to invite the Soviet Union into the principal international financial institutions. Once they're in the IMF, they're in it, and you don't

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take them out if things then change later on or if Mr. Gorbachev fails and is replaced later on.

So I think we want to be very careful about making permanent structural concessions that we can't recover if things begin to deteriorate.

Representative PORTER. Thank you very much.

Mr. Chairman, thank you.

Chairman HOYER. Thank you. I have 33 more questions, and you just heard the bell rang. In any event, I couldn't ask all those questions. Many of them have been asked.

I want to say to each one of you that I think this has been one of the most interesting, informative, and important hearings that the Helsinki Commission has held in some time.

This is an area that is difficult to grapple with, and I think the friction that exists between the private and public sector agendas is clearly one with which we're going to have to deal. I think it's one that we're going to have to have a lot more discussion about. I'm glad that you were here.

By the way, I want to say, Mr. Bonsignore, I think you did respond to exactly what we asked you to respond to. Don't take any umbrage at Congressman Kemp's observations, which I also think are a concern he reflects about this sometimes dichotomy, sometimes friction——

Mr. BONSIGNORE. I know.

Chairman HOYER [continuing]. Sometimes hopefully cooperation between the public and private sector agendas.

But I want to thank each one of you, Richard Perle, Paula Stern, Roger Robinson, and Mr. Bonsignore, for being with us. I'm also appreciative of Secretary Verity.

We're going to pursue this, further, and I think that probably we'll be talking to you privately as well as we try to fashion both public policy and private initiatives and closer cooperation between the two.

Thank you very, very much.

[Whereupon, the foregoing hearing was concluded at 4:49 p.m.]

APPENDIX I

STENY H. HOYER, MARYLAND, CHAIRMAN

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COMMISSION ON
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June 9, 1988

The Honorable C. William Verity
Secretary
United States Department of Commerce
14th and Constitution
Washington, DC

Dear Mr. Secretary:

Pursuant to the excellent and informative exchange of ideas which took place during your testimony before the Helsinki Commission on May 12, I should like to follow through with a few questions on behalf of myself and my colleagues which you kindly agreed to respond to in more detail after the hearing.

1. I was particularly interested in knowing what types of products might be imported from the Soviet Union if MFN were to be granted. In consultation with you during the hearing, Mr. Vargo indicated that a survey of this type hadn't been done in some time. Do you anticipate conducting such a survey in the near future? Absent such a survey can you provide a list of the types of products which we <u>might</u> expect to see?

2. Senator D'Amato requested a copy of the standards test the Department of Commerce now uses in determining if products being imported from the Soviet Union may have been produced by forced labor. You indicated to the Senator that <u>you</u> would be happy to provide that test. We should like to request it at this time.

3. Finally, Senator Wirth expressed an interest shared by many of us regarding a "criteria against which we can state what is important and what isn't important " with respect to policy governing trade relations with the Soviet Union. Senator Wirth referred to human rights considerations beyond just emigration. In that regard, does the Department of Commerce have an established, articulated policy regarding Jackson-Vanik? Is the focus, for instance, on numbers or is it based on the institutionally-protected right of an individual to emigrate? At what point would the Department of Commerce recommend waiving Jackson-Vanik? Would a significant increase in numbers justify this or would the policy be set against an effective change in Soviet law which would guarantee the right of the individual to leave his or her country? Would other human rights considerations come into

play such as the release of political prisoners or the right of citizens to form, among other organizations, Helsinki monitoring groups?

In addition to providing Senator Wirth with a response to his concerns, your thoughts on this matter will be helpful to all the members of the Commission in this era of growing detente with the Soviet Union.

On behalf of all of us on the Commission, we again wish to thank you for taking the time to participate in the trade hearing. Your contribution was extremely valuable. We look forward to hearing from you at your earliest convenience.

Sincerely yours,

Dennis DeConcini

DENNIS DeCONCINI
CoChairman

APPENDIX II

THE SECRETARY OF COMMERCE
Washington, D.C. 20230

JUL 13 1988

Honorable Dennis DeConcini
Cochairman, Commission on Security
and Cooperation in Europe
United States Senate
Washington, D.C. 20515

Dear Mr. Chairman:

Thank you for your letter regarding additional information to follow up on the testimony I gave before the Helsinki Commission on May 12. I am pleased to respond in greater detail to these questions.

The first question concerns the types of commodities the Soviets might export to the United States were they to be granted most-favored-nation (MFN) tariff treatment. In general, it is difficult to make such estimates because of factors such as the often lower-than-Western standards of quality of Soviet manufactured output and questions as to whether an already overtaxed Soviet manufacturing sector could increase production to supply a new market.

A 1977 report by the International Trade Commission (copy enclosed) concluded that it was unlikely that U.S. imports would increase substantially under MFN merely because the tariff rates assessed against Soviet products would then be lower. Most products which the Soviet Union exports to the West do not encounter significant tariff discrimination in the U.S. market. Because the structure of Soviet exports has not changed since the 1970's, I believe the report's conclusions are still valid.

Enclosed is a list of several products which the Soviets might try to export to the United States if they were granted MFN. These products are selected from United Nations statistics on trade of manufactured goods in 1986 between the Soviet Union and Western Europe and Japan (countries which have extended MFN to the Soviet Union) because they are shipped with some regularity from the Soviet Union, have a relatively high total value, and would be subject to an MFN duty significantly lower than the column 2 duty which currently applies. Goods on this selected list comprised only three percent of Soviet exports of manufactured goods to Western Europe and Japan in 1986.

Your second question concerns the standards test used to determine if imported goods have been produced under forced labor. The jurisdiction for this issue falls to the Department of the Treasury and is legislated by section 307 of the Tariff Act of 1930. I am enclosing the implementing language from U.S. Customs Regulations.

Regarding our policy on the Jackson-Vanik Amendment, I made it clear to the Soviets in Moscow that the Amendment represents, and will continue to represent, the policy of the United States. I said that I was encouraged by improvements in the area of human rights and emigration and hope that they will lead to a great deal more.

Urging the Soviets to make a breakthrough, I said they should apply "glasnost" to emigration by removing quotas and requirements for family approval and by having reasonable waiting periods for those in security sensitive positions. With those changes, and with a substantial and sustained increase in emigration numbers, a Jackson-Vanik waiver might be considered in the future. However, Soviet policy and actual practice must change. Specific conditions for seeking a waiver under Jackson-Vanik would have to be determined by the President, based on advice of the Secretary of State and other Cabinet members and progress in achieving the goals of the Amendment, including emigration and human rights.

Sincerely,

Secretary of Commerce

Enclosures

Legal Elements and Evidentiary Standards for Application of 19 U.S.C. §1307, Prohibiting the Importation of Convict-Made Merchandise

I. The Statute

The operative sentence of section 1307 provides:

> All goods, wares, articles, and merchandise mined, produced, or manufactured wholly or in part in any foreign country by convict labor or/and forced labor or/and indentured labor under penal sanctions shall not be entitled to entry at any of the ports of the United States, ...

An exception, applicable where domestic U.S. demand is not being satisfied, will be quoted and discussed later.

II. The Procedures

A. The Secretary of the Treasury has substantive authority to make "such regulations as may be necessary for the enforcement of this provision." In the exercise of that authority, he has promulgated regulations defining the procedures the Commissioner of Customs is to follow in enforcing section 1307. See 19 C.F.R. §12.42-.44.

B. On receiving written information sufficient to support a decision and after such investigation as is warranted, id. §12.42(a)-(d), if the Commissioner finds "that information available reasonably but not conclusively indicates that merchandise within the purview of section [1307] is being, or is likely to be, imported, . . . the district directors shall thereupon withhold release of any such merchandise . . . ." Id. §12.42(e).

C. If the Commissioner actually determines "that the merchandise is subject to" section 1307, he is to obtain the approval of the Secretary of the Treasury and publish "a finding to that effect" in the Federal Register and the Customs Bulletin. Id. §12.42(f).

D. Any particular entry of merchandise that is (1) within a "class specified in a finding made under paragraph (f)", and (2) still being detained by Customs at the time of the publication, is to be treated as "an importation prohibited by section [1307]" unless the importer is able to establish "by satisfactory evidence that that particular entry of merchandise was not mined,

produced, or manufactured in any part with the use of a class of labor specified in the finding." Any importer, it appears, may voluntarily export the detained merchandise at any time.

E. Absent voluntary exportation, the Customs Service must hold the merchandise until 3 months after the publication or until 3 months after the attempt to import the merchandise, whichever is later. Up until that time, the importer may bring in evidence to establish that the particular merchandise at issue was not made with the use of a class of labor specified in the finding. Id. §12.42(g).

F. If satisfactory proof has not been submitted within 3 months, Customs is to notify the importer "in writing that the merchandise is excluded from entry". After waiting an additional 60 days to permit the importer to export the merchandise or file an administrative protest under 19 U.S.C. §1514, Customs is to treat the merchandise as abandoned and destroy it.

III. The Legal Elements and Evidentiary Requirements

A. While section 1307 only prohibits the entry of merchandise that actually contains "wholly or in part" components made with prohibited labor, the Secretary has substantive rulemaking power permitting him to detain other merchandise if reasonably necessary to achieve that purpose.

B. The responsibility of the Commissioner (to whom authority to implement the regulations has been delegated) is to make preliminary and (with the approval of the Secretary) final findings concerning whether merchandise is being or is likely to be imported in violation of section 1307. There is no provision granting any importer a right to participate at this stage of the process. In making those findings, under §12.42(e) and (f) of the regulations, both the detailed requirements of §12.42(b) and the protest and judicial review provisions of §12.44 cause us to conclude that the findings must be supported either with (a) a recitation of the evidence and reasons supporting it or (b) the detailed supporting material required to be submitted to the Commissioner under §12.42(b), supplemented with the results of any further investigation he undertakes. This requirement, however, does not require that he reveal classified information and it is expressly contemplated that, should judicial review be sought at any point, the Government should reserve the option of protecting its intelligence sources and methods even at the cost of loss of the litigation. Appropriate unclassified summaries should be substituted to support the findings.

C. 1. Upon receiving information as provided in the regulation, the first step that the Commissioner must take is to define the appropriate class of merchandise. The Commissioner

has the authority to proscribe the entry of "goods, articles or merchandise" through the use of administratively necessary classifications. That is, he is empowered (as a result of his substantive rulemaking authority under section 1307) to define categories of merchandise that are to be detained or excluded despite the fact that a particular class may be somewhat too narrow or too broad to coincide perfectly with the universe of merchandise that was actually produced with convict, forced, and/or indentured labor.

C. 2. In establishing each such class, the Commissioner should use the narrowest classification that he can reasonably establish. That is, by using the most specific Tariff Schedule classification possible, and/or narrowing limitations such as country of origin, manufacturer, or specific physical characteristics, he should seek to avoid prohibiting the entry of any merchandise that is not necessary to the task of excluding the prohibited merchandise. Where possible he should use multiple narrow classifications rather than a single broad one.

D.1. Under the statute and regulations, merchandise is only excludable if it contains "wholly or in part" components made with prohibited labor. That is, the use of tools, factories, energy, or other means that were themselves made with prohibited labor to produce the merchandise will not make the merchandise excludable. In addition, the merchandise is excludable if any part or component is made with prohibited labor, except where the part or component is de minimus. Such a rule would comport with the construction given by the Court of International Trade to the term "in part." It would also permit the Treasury to invoke more easily the 1307 exclusion and shift to the importer and producer the burden of proving that the imported article is not "in part" of the offending component by establishing that the economic contribution of the prohibited labor to the article is de minimus.

D.2. The legislative history of the statute reflects the intent of Congress to protect American industries from foreign competitors who obtain a competitive advantage by using forced labor. Therefore, with respect to any producer in a free market economy for which such information is available, the Commissioner should make a specific finding that the use of forced labor gives that foreign producer a more than de minimus price advantage over American producers. If such information is not available because either the foreign producer or the country in which it is located is unable or unwilling to make such information available or is unreliable because the producer is in a state controlled economy in which costs and prices can be artificially set, then the Commissioner should consider the following in determining whether a competitive advantage resulting from the use of forced labor is more than de minimus:

(a) whether the economy is free market or state controlled;

(b) the nature of the product (whether labor cost is a significant component);

(c) the (apparent) value added by use of forced labor;

(d) the number of parts added or assembled by use of forced labor, relative to the number of parts in the finished product;

(e) the percentage of time required for production of the article which is contributed by forced labor; and/or

(f) any other relevant information available.

E. 1. If the class established is excessively overbroad, that is, if it includes too many articles that are not subject to the statutory prohibition, it cannot be justified under the rulemaking authority of the statute. A de minimus rule -- to the effect that goods will only be excludable under section 1307 if the classification chosen is not too overbroad -- should be developed on a case-by-case basis. In order to ensure that this important limitation is actually considered and applied in each case, the question of the overbreadth of each class should be expressly addressed in quantitative terms in each preliminary and each final finding. This step will help avoid a principal cause of the lack of uniformity in our past findings in this area. This is not to say that unrealistic precision should be artificially imposed on information that will not support it. But quantitative ranges (e.g., between 30 and 50%), rather than vague qualitative terms ("substantial" or "small") are needed, and the best estimate that is possible under the circumstances should be stated in the Commissioner's findings.

E. 2. The determination of the amount of overbreadth to be permitted is a judgment that should be made by the Secretary, or his delegee. So long as the overbreadth in each classification has been quantified to the extent that the available information reasonably permits, case-by-case application of the statute and regulations should lead to the evolution of more consistent standards than our past practice. This approach must permit the use of different quantitative standards where a country or other entity refuses to permit the Commissioner to perform an adequate investigation.

F. In deciding whether to act, the Commissioner must determine whether prohibited merchandise of the class defined "is

being or is likely to be" imported. Although research failed to reveal any case in which this language was invoked absent an actual importation -- with the resulting inference that additional merchandise was likely to be imported -- there is no indication in the statute, regulation or legislative history that such a limitation was intended. It seems fair to interpret the word "likely" in accordance with the dictionary definition "reasonably to be expected," and not to read into it any more stringent standard implying that importation must be more likely than not.

G. 1. The Commissioner must then determine whether the exception in section 1307 for "goods, wares, articles, or merchandise ... not mined, produced, or manufactured in such quantities in the United States as to meet the consumptive demands of the United States" is applicable to any of the classes he has defined. The words "consumptive demand" cannot be read to mean demand at a price influenced or potentially to be influenced by importation of the prohibited merchandise, or the entire statute would be nullified and its purpose not served. Under the circumstances, it seems consistent with the statute only to apply it where there is no possibility of domestic production or what little there is cannot be significantly expanded even at a manyfold increase in price.

G. 2. The exception should use all domestic merchandise that fits within the classification that is selected for the finding (presumably stripping out the country-of-origin and, where applicable, manufacturer limitations), and should also take account of any commercially viable substitutes available in the domestic economy.

APPENDIX III

STATEMENT OF SENATOR ALFONSE D'AMATO
BEFORE THE COMMISSION ON SECURITY AND COOPERATION IN EUROPE
HEARING ON "SOVIET TRADE AND ECONOMIC REFORMS:
IMPLICATIONS FOR U.S. POLICY."
MAY 10, 1988

MR. CHAIRMAN, I WANT TO BEGIN BY THANKING YOU AND OUR DISTINGUISHED CO-CHAIRMAN, SENATOR DECONCINI, FOR SCHEDULING THIS HEARING ON THE IMPORTANT TOPIC OF "SOVIET TRADE AND ECONOMIC REFORMS: IMPLICATIONS FOR U.S. POLICY." THE WITNESSES APPEARING BEFORE US TODAY, INCLUDING THE SECRETARY OF COMMERCE, MR. C. WILLIAM VERITY, ARE WELL-QUALIFIED TO REVIEW THIS TOPIC FOR US. I LOOK FORWARD TO THE OPPORTUNITY TO DISCUSS WITH THEM THE ISSUES FACING US AS GORBACHEV'S REFORMS PROCEED AND AS PRESSURES INCREASE TO EXPAND U.S. - SOVIET TRADE.

I WANT TO SPEAK TO ONE OF THOSE ISSUES, THE ISSUE OF EMIGRATION FROM THE SOVIET UNION. WE NEED ANSWERS TO THIS KEY QUESTION BEFORE U.S. - SOVIET ECONOMIC RELATIONS CAN IMPROVE SUBSTANTIALLY. THE JACKSON-VANIK AMENDMENT LINKED SUCH TRADE IMPROVEMENT TO BETTER SOVIET EMIGRATION PERFORMANCE.

SECRETARY VERITY'S PRESENCE HERE TODAY IS PARTICULARLY WELCOME. I OPPOSED HIS SENATE CONFIRMATION ON THE BASIS OF HIS PAST REMARKS REGARDING THE RELATIONSHIP BETWEEN HUMAN

RIGHTS AND U.S. - SOVIET TRADE. AT THAT TIME, HE GAVE ASSURANCES OF HIS SUPPORT FOR THE PRESIDENT'S POLICY ON EMIGRATION AND HUMAN RIGHTS. HAVING HAD THE OPPORTUNITY TO SEE WHAT OCCURRED ON SECRETARY VERITY'S APRIL VISIT TO THE SOVIET UNION, I CAN SAY THAT HE IS A MAN OF HIS WORD. HE TOOK A STRONG, PUBLIC STAND FOR THE PRINCIPLE EMBODIED IN JACKSON-VANIK -- THAT THERE CAN BE NO MARKED IMPROVEMENT IN U.S. - SOVIET TRADE RELATIONS UNTIL THE SOVIETS KEEP THEIR INTERNATIONAL COMMITMENTS CONCERNING EMIGRATION.

MR. SECRETARY, LET ME SAY I APPRECIATE THE STAND YOU TOOK. ON BEHALF OF SUPPORTERS OF HUMAN RIGHTS HERE, IN ISRAEL, IN THE SOVIET UNION, AND AROUND THE WORLD, I THANK YOU FOR YOUR GOOD EFFORTS.

LAST MONTH'S SOVIET JEWISH EMIGRATION NUMBERS ARE UP. A TOTAL OF 1,088 PEOPLE WERE ALLOWED TO LEAVE. THIS IS AN IMPROVEMENT, BUT STILL, ON AN ANNUAL BASIS, IT WOULD MEAN THAT ONLY A LITTLE MORE THAN 13,000 PEOPLE WOULD BE ALLOWED TO LEAVE. MEASURED AGAINST SOVIET EMIGRATION PERFORMANCE IN THE LATE 1970'S, UNDER JACKSON-VANIK, THIS IS CLEARLY INADEQUATE.

AS I HAVE OFTEN SAID, I AM PREPARED TO SUPPORT MODEST INCREASES IN NON-STRATEGIC U.S. - SOVIET TRADE, TO ENCOURAGE CONTINUING SOVIET IMPROVEMENT IN COMPLIANCE WITH THEIR

INTERNATIONAL OBLIGATIONS. I AM NOT, HOWEVER, PREPARED TO ACCEPT SUGGESTIONS FOR WAIVER OR REPEAL OF JACKSON-VANIK OR THE STEVENSON AMENDMENT UNTIL SOVIET PERFORMANCE RISES AT LEAST TO LEVELS IT ATTAINED IN THE PAST.

IN THE LONGER RUN, WE CANNOT ALLOW PURSUIT OF PROFITS TO BLIND US TO CONTINUED, FLAGRANT VIOLATIONS OF OUR FUNDAMENTAL PRINCIPLES -- PRINCIPLES THAT THE SOVIETS ACCEPTED WHEN THEY SIGNED THE HELSINKI ACCORDS. SOVIET REFORMS MUST REACH THOSE HUMAN RIGHTS ISSUES THAT STILL MAKE THE NOTION OF A MOSCOW HUMAN RIGHTS CONFERENCE A BAD JOKE.

WE CAN AND MUST ENCOURAGE THOSE ASPECTS OF GENERAL SECRETARY GORBACHEV'S REFORMS THAT HELP BRING THE SOVIET UNION INTO COMPLIANCE WITH ITS INTERNATIONAL HUMAN RIGHTS OBLIGATIONS. BUT ENCOURAGEMENT MUST BE GIVEN WITHOUT GIVING AWAY THE STORE. OTHERWISE, WE MAY FIND WE HAVE MADE CONCRETE ECONOMIC CONCESSIONS WITH IRREVERSIBLE IMPACT, IN EXCHANGE FOR HUMAN RIGHTS COMPLIANCE STEPS THAT CAN BE REVERSED LITERALLY OVERNIGHT.

I LOOK FORWARD TO THIS OPPORTUNITY TO DISCUSS THIS ISSUE WITH SECRETARY VERITY, DR. STERN, MR. ROBINSON AND MR. DOWLIGNORE.

THANK YOU, MR. CHAIRMAN.

APPENDIX IV

THE HONORABLE PAULA STERN, SENIOR ASSOCIATE

CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE

STATEMENT BEFORE THE COMMISSION ON SECURITY AND COOPERATION

IN EUROPE,

DIRKSEN SENATE OFFICE BUILDING

MAY 10, 1988

UNITED STATES-SOVIET TRADE: THE QUESTION OF LEVERAGE

United States-Soviet Trade: The Question of Leverage

by The Hon. Paula Stern

Senior Associate, The Carnegie Endowment for International Peace

May 10, 1988

Testimony submitted to the Helsinki Commission

Chairman Hoyer, Co-Chairman DeConcini, members of the Commission, thank you for giving me the opportunity to testify before this hearing on US-Soviet trade in the context of the upcoming summit in Moscow.

Whenever US-Soviet political relations begin to warm, Washington officials get busy developing scenarios for removing barriers to trade with the Soviet Union. The most prominent example of this phenomenon occurred in the era of detente in the early 1970's culminating in the trade agreements signed at the May 1972 summit in Moscow between Richard Nixon and Leonid Brezhnev. This impulse last took hold at the time of the signing and consideration of ratification of SALT II in 1979.

Now, on the eve of the May, 1988 summit between President Ronald Reagan and General Secretary Mikhail Gorbachev, comes another thaw and another shake of the trade thermometer to take the temperature of our relationship. And once again, economic leverage on the USSR has surfaced as a foreign policy issue. The intriguing question is whether Mikhail Gorbachev's need to buy time at home by increasing the supply of food and consumer goods to its citizens in order to facilitate perestroika's (restructuring) provides a promising new target of

political opportunity for the United States.

The purpose of this hearing is to discuss the utility of using economic leverage to encourage Soviet human rights compliance. I am here to tell you that while trade is a handmaiden of politics, it is a weak one, and it works best when it is a carrot not a stick. Our leverage is limited first and foremost by economic constraints of US-Soviet trade itself. Trade matters less to the Soviet Union, which tends to be autarchic, than it does to the United States, which is increasingly economically interdependent. In effect, the Soviets can and do turn off the spigot anytime. Trade between the two nations is small, unbalanced, and composed mainly of raw materials, particularly grain. United States is constrained by domestic political groups, namely farmers, when it comes to grain. Moreover, as the grain embargo post Afghanistan suggests,it is difficult to get a united political position in the West when sanctions are imposed.

What is meant by economic leverage? Klaus E. Knorr, the political economist, wrote several volumes on the subject. But simply stated, it is the use of economic muscle to advance political ends. The possibility of using economic tools -- instead of military machines -- is obviously more attractive in US-Soviet relations because both countries' nuclear capacity makes military confrontation suicidal. Furthermore, economic tools may be used continuously and in an almost unlimited number of combinations. Yet, the fact that both the United States and

the Soviet Union are economic superpowers and leading advocates of distinct economic systems multiplies the complexities of attempting to exercise economic leverage.

Commercial relations between the United States and the Soviet Union have never been a simple matter of dollars and cents. They have been the source of political tension -- as well as the means of expressing political tension generated by other issues. In short, trade is the anemometer that gauges the prevailing political winds between Moscow and Washington.

Over the years, US officials have generally assumed that leverage could be used, but the historical results of attempting to apply it have been disappointing. US history is littered with examples of government officials trying to use trade to elicit a desired political response from Russia and subsequently the Soviet Union.

Trading with a nation is desirable, so its gives some political leverage. So repeatedly the question that gets asked is not "if" but "how" the US can exert leverage. Adroit negotiating, therefore, might result in some additional marginal political advantage for the United States derived from the Soviet desire for U.S. goods, and access more generally to Western financing, international markets and the latest technological know-how.

While past attempts by the United States to wield economic leverage have generally been disappointing, a review of historical patterns and benchmarks can guide policymakers around

future pitfalls. A brief historical scan highlights how most-favored-nation tariff treatment (MTN), financial credits, export licenses, debt resettlement, and grain sales have been used as instruments of trade politics. Certainly there are lessons here for 1988 and this new detente.

HISTORICAL SURVEY: TOOLS OF THE TRADE

In 1832, the United States and Russia signed their first formal trade agreement, which provided for most-favored-nation tariff treatment. By 1912, the United States had revoked the treaty in protest of Russian mistreatment of naturalized American Jewish citizens making return visits to their Russian homeland. MFN was granted again in 1933, almost revoked a year later, and conclusively revoked in 1951.

The United States has also used export licenses, agricultural sales, and government-issued credits from the Export-Import Bank and the Commodity Credit Corporation to influence Soviet behavior. Government issued commercial credits, such as loans from the Export-Import Bank and the Commodity Credit Corporation (The former was established initially in the early 1930's for the primary purpose of financing trade with the newly recognized Soviet state.) to finance exports to the USSR, as well as export licenses have been similarly manipulated at different periods to influence Soviet behavior in both economic and noneconomic fields. They have been used to encourage repayment of Czarist debts from World War I and later lend-lease

debts from World War II, to restrain Communism's ideological incursions into the domestic political debate in the United States after World War I and later in Western Europe after World War II, and at the same time to discourage Russian military and political expansion, particularly in Eastern Europe.

Grain sales have also attracted the attention of those who would attach political conditions to trade relations. When the administrations of John Kennedy and Lyndon Johnson resisted conditioning grain sales on broad areas of Soviet behavior, 1964 Presidential contender Richard Nixon criticized that restraint. Subsequently when Nixon was president in the 1970's, he based much of his Soviet policy on the assumption that Soviet need for Western goods and technology would make the USSR more cooperative, even insofar as assisting American efforts to extricate itself from the Viet Nam War. Historical evidence suggests, however, that he made no effort to attach conditions to the Soviets' great grain purchases of 1972 because the magnitude and timing of the sales were a mystery to American foreign policymakers.

Many of America's efforts to harness US economic power for political ends have had disappointing results. Abrogation of the commercial treaty in late 1911 did not achieve its intended objective. From 1917 to 1920, American cooperation with the Allied economic blockade of the new Bolshevik regime yielded as little as did Allied military intervention. Attempts in 1933 to use prospects of credits and increased trade with Russia as a

restraint on communist activities were not very productive. Moreover, efforts to use reconstruction loans and settlement of World War II lend-lease debts to restrain the Soviet Union in Eastern Europe and elsewhere probably hardened the attitudes of the Russian leadership against cooperation with the West. The Cold War's strategic embargo which peaked in 1953 froze an already difficult relationship.

HISTORICAL SURVEY: EXAMPLES OF LINKAGE

Looking in greater detail at more recent examples of linkage will shed more light on the question of the utility of using economic leverage to advance other areas of national concern.

Detente and "Parallelism"

The United States is now into the 1988 presidential campaign period and on it is the eve of a May summit in Moscow. In another presidential campaign year, 1972, there was another May summit in Moscow -- when detente bloomed between Richard Nixon and Leonid Brezhnev. In 1972, "parallelism," a term coined during the Nixon-Kissinger era, was being practiced as an economic corollary to linkage.

The Nixon Administration assumed that Soviet need for Western goods and technology would make the USSR a more cooperative negotiating partner, even to the extent of aiding American efforts to extricate the US from the Vietnam War. Nixon's electoral mandate in 1968 was to get the US out of the

Vietnam War; the final deadline was no later than reelection time 1972. Even in his first news conference as president, Nixon made it clear that he would try "to woo the Russians into a new and cooperative approach to a Vietnam compromise by dangling attractive bait before them - SALT, trade, and easing of tensions around Berlin, a European security conference."

His administration tried to pace its liberalization of existing trade restrictions. First, it granted more licenses for export to the Soviet Union. Then, during negotiations on other subjects, it held out the possibility of extending credits and most-favored-nation tariff treatment. Kissinger, however, insisted that his linkage approach was more subtle than demanding a strict quid pro quo for American trade concessions: "I am denying that we ever said to the Soviet leaders, 'If you do this for us in Vietnam, we will do that for you on trade.' You have to recognize that these are serious people and we didn't come to buy them."

Ironically, Nixon, Kissinger, and their colleagues were not fully aware of one of their greatest opportunities to use economic leverage for political purposes. In July and August of 1972, Soviet officials purchased huge amounts of grain in this country before Kissinger knew enough about Soviet needs to capitalize on them. Even though the United States did not forge a conscious link at the time, the Soviets themselves -- aware of their vulnerability during the grain-short year of 1972 -- may have been more cooperative vis-a-vis American efforts to get a

Vietnam peace agreement. The Nixon Administration did, however, consciously encourage Soviet agricultural growth with Ex-Im Bank-financing for Occidental Petroleum's $20 billion ammonia-superphosphate deal.

If we consider the May 1972 Summit where SALT I, trade and other agreements were either signed or initialed as the launching of detente, then it could be argued that the ship of trade never left the port. Even as Nixon was meeting with Brezhnev, Senator Henry Jackson was developing legislation tying MFN tariff treatment and access to government exports credits and credit guarantees to a specific political demand on the Soviet domestic system: freedom of emigration for its citizens.

The Jackson Amendment

The Jackson amendment to the Trade Act of 1974 was an explicit harnessing of U.S. economic might in order to gain a moral and political objective inside the USSR. It said, in effect, "if you do this for us, we will do this for you," and it failed. In 1975 and again in 1976, the two years after the amendment became law, only fourteen thousand Jews left the Soviet Union. That was a decrease from the 1973 high of almost thirty-five thousand and the lowest rate since 1971. There are a number of reasons why actual passage of the amendment did not work. Not the least of them was Moscow's resentment of Jackson's public advertisement of his purported success with the Soviets. The boasting served to undermine the objective. It should be

remembered, too, that by 1974, actions taken by OPEC sent the price of petroleum soaring and gave the oil exporting nation of the Soviet Union new economic clout.

The Stevenson Amendment

Passage of the 1974 Stevenson amendment to the Export-Import Bank Bill, which is also still on the books, compounded the insult of the Jackson amendment. The Stevenson amendment attempted to use export credits to influence a wider range of political goals. Instead of a blanket prohibition against extending credits, it put a ceiling of $300 million on new credits and gave Congress authority to review all Ex-Im Bank transactions of more than $50 million.

The Stevenson Amendment was adopted by the Congress without any attempt by Nixon or Kissinger to use it as a substitute for the Jackson amendment, the role Stevenson had initially meant it to play. As a result, the flexible use of economic leverage against the Soviet Union was effectively denied to US policymakers, while at the same time US businessmen were denied the benefits derived from MFN status and export credits for the Soviet Union.

The Jackson and Stevenson Amendments were passed as amendments to the Trade Reform Act which President Gerald Ford signed in January 1975. Those provisions tied not only his hands but those of all future Presidents who have looked for ways to use trade as a flexible and subtle lever on the Soviet Union.

The Ford Administration: the Last Straw

After the Jackson Amendment became law, President Ford turned to grain, negotiating a five-year minimum sales agreement with the USSR. US-USSR trade statistics fluctuated with the USSR's grain harvest. When the Soviet Union suffered a severe harvest failure in 1978, for example, trade reached a new peak.

Afghanistan Invasion Sanctions

The major trade weapon remaining in America's arsenal when the Soviets invaded Afghanistan in December, 1979 was grain. For technical legal reasons, President Jimmy Carter's efforts to shelve the Occidental Petroleum ammonia fertilizer deal was frustrated. Carter imposed a partial embargo on future grain exports, excluding the eight-million-ton minimum guaranteed under the 1975 US-USSR long-term grain supply agreement. The Soviet economy was believed to be particularly vulnerable because it had experienced another crop failure in 1979 and then a mediocre harvest in 1980.

By April of 1980, the Soviets reached the ceiling of the US-USSR grain agreement, but still 75 percent of its imported grains needs remained unsatisfied. The US obtained the support of several grain-exporting countries in the embargo, including the European Economic Community, Australia, and Canada, who agreed not to replace shortfalls caused by US sanctions. However, Argentina did not support the embargo, and in late 1980, Canada

also agreed to supply additional grain to the Soviets in 1981. Meanwhile, 1980 was a particularly good year for Soviet exports because the world prices of crude oil, gold, diamonds, and other precious minerals were extremely high. So the USSR was able to amass large hard currency reserves and pay premium prices wherever grain was for sale.

In retrospect, the grain replacement opportunities for the Soviets turned out to be better than originally expected. The Soviets did experience some shortfalls that necessitated heavier than normal slaughter of animals and resulted in scarcity of food, particularly milk and dairy products. Nevertheless, the Soviet Union was able to absorb this shortfall, and the embargo did not appear to have had a significant effect on Soviet policy regarding Afghanistan.

The Reagan Administration

In April 1981, Reagan -- keeping a campaign promise -- lifted the grain embargo in spite of the continued Soviet involvement in Afghanistan and the simmering Polish government crisis. Reagan's first Secretary of State Alexander Haig -- who learned much about trade linkage on Kissinger's National Security Council staff during the Nixon Administration -- opposed this decision, arguing that the timing of the revocation of the embargo was diplomatically unjustifiable.

In December, 1981 Poland declared martial law. Citing Soviet complicity, but having stripped himself of even the grain

weapon, Reagan was left with the symbolic gesture of suspending the negotiations on renewing the five-year grain agreement. The Reagan Administration also suspended issuance of export licenses for certain high technology goods, specifically oil and gas equipment, and expanded the list of such equipment requiring a license. Aimed at disrupting the progress of the natural gas pipeline between the USSR and Western Europe, these actions brought tensions between US and Europe on East-West trade policy to an all time high. With this act, Reagan absolutely reversed the US position on Soviet energy development which Nixon's detente policy had vigorously supported. For the first time since the West's Cold War strategic embargo of Stalin's USSR, allied cooperation on trade sanctions became a critical alliance issue.

In June, 1982 Reagan's pipeline proposals received a very lukewarm response at the Versailles Summit. The next month, the United State's extraterritorial extension of the embargo on oil and gas equipment to include subsidiaries and licensees of US companies infuriated Western European allies. By November, 1982 the pipeline sanctions were revoked while the Europeans agreed to tighten government-supported credit terms for the Soviet Union, to explore means to lessen energy dependence on the Soviet Union, and to improve coordination of technology transfer with a view to making it more difficult for the Soviets to obtain technology with military applications. At the Williamsburg Economic Summit, the allies did not resolve their differences over America's

embargo policy.

The Soviet economy turned down in 1982, principally because the price of oil and gold fell precipitously. Its oil production peaked, and heavy domestic demands left less available for export. Thus, the Soviets' hard currency reserves dwindled, making it more difficult for them to import needed grain and high technology. The natural gas pipeline was therefore an important objective in their plans for long-term economic growth.

Some, such as Secretary of Defense Weinberger, suggested at the time that the Soviet's economic downturn was evidence of a "window of opportunity" for the exercise of US economic leverage. In other words, it was assumed that the Soviet economy was again sufficiently vulnerable that the exercise of Western trade muscle could force the Soviets to desist from their military and nuclear arms buildup. At least, it was thought, the United States could impose a harsher choice between guns and butter by denying the USSR technology and credit, particularly with respect to the pipeline. Some went so far as to say that destabilization caused by tough Western measures could result in meaningful domestic reform as well.

President Reagan's decision in November of 1982 to lift the pipeline-related sanctions was a drawing back from the Weinberger position. The US recession made US business eager for sales and the Administration gave way. A domestic political imperative had once before impelled Reagan away from trade sanctions -- the grain embargo -- when it became unpopular.

American farmers had been suffering from the lowest real income and greatest bankruptcy rate in a quarter century. The surplus grain looked a lot like the mountain of grain that Nixon's Agriculture Secretary Earl Butz had tried to peddle in 1972. And businessmen suffering from a severe recession in 1982 were also anxious for a chance to sell -- echoes of businessmen trying to gain new markets in the USSR during the 1971 recession.

The trade thermometer was registering warmer relations for the superpowers. By appearing more amenable to negotiations with the Soviets, Reagan was easing the concerns of American voters, farmers, businessmen, and his Western allies. He broached the notion of a summit with Andropov. He proposed -- and the Soviets accepted -- negotiating a new long-range grain agreement.

The accumulated history of the early 1980s show attempts to use punitive leverage increasingly left the US out of trade with the USSR. Japan and Europe picked up the industrial trade in the energy development field -- in compressors, submersible pumps, large diameter pipes, pipelayers, etc. The US played a declining role in grain with the US being a supplier of last -- not first -- resort while Canada and Argentina played the role of main suppliers under long-term agreements.

What were the lessons from those latest attempts to apply economic sanctions? First, the price paid by the United States, and particularly the US agricultural community was greater than it was during detente when economic diplomacy was all carrot -- a carrot of gold -- golden grain for the Russians, money in the

pocket for the farmers, a Nobel Prize for Kissinger, reelection for Nixon.

Second, the vulnerability of the Soviet economy may have been overestimated.

Third, one major "lever" that was chosen -- grain -- turned out not to have as much clout as was thought. Using the supplier-client analogy, the effectiveness of a supplier's restrictions on a client is obviously undermined to the extent that the supplier itself needs to make the sale. In addition, assuming that political goals justify such losses, the Afghanistan incident suggests that a fungible, multiple-sourced commodity such as wheat and other grains is a poor "lever" to use. It is downright impossible if the farm bloc blocks its use. And you cannot get a hand on that lever if the farm bloc wields sufficient clout.

So post-Afghanistan, US policymakers concluded that it was better to try to use "unique" products, such as high technology items in the oil and gas field. And what lessons can be gleaned from the exercise of leverage by means of oil and gas industry technology restraints? The sanctions imposed by the US and its allies cannot be called flatly ineffective because the Soviet Union did not, in fact, intervene militarily in Poland. However, the importance of the trade sanctions, as opposed to other factors, cannot be known. There are indications, however, that one important factor restraining the Soviets was indeed that both West Germany and France "hinted" that the future of the pipeline

would be jeopardized by intervention. Quiet "hints" worked better in all likelihood than public threats.

The most striking lesson here is that more weight must be given to whether our allies are willing to join in efforts to use leverage. The Polish initiative required too great an economic sacrifice for the Europeans -- a sacrifice, they claim, the US was not willing to make itself. The US rejoinder was that grain can be replaced by other countries, but that some of the oil and gas technology could not. Another fundamental problem with the "Polish" sanctions was that they did not appear to be specifically tailored to the question of Poland, but were an attempt to impose broader US objectives regarding the pipeline which the allies did not support.

The Polish situation further bore out the fact that a supplier in serious economic need of making a sale lacks the clout to impose effective trade sanctions.

The pipeline sanctions meant considerable expense for the US companies involved. Moreover, they required the ailing European economies to forego a vital interest. Finally, the Polish sanctions suggested that one underlying assumption of leverage -- that the United States had superior economic muscle that could be translated into political muscle --must give way to the recognition that the Western economies -- the United States included -- are becoming more interdependent.

ECONOMIC CONSTRAINTS ON FUTURE TRADE

I have described the political nature of this relationship at considerable length. Economics was, is, and always will be a handmaiden of the politics of the superpowers. The domestic politics of the two nations will shape the trade relationship. And the unique characteristics of superpower politics forces the trading relationship into a bilateralism that departs from the multilateralism that otherwise has been a underlying principle of US trade policy.

But even if politics dominates the past and existing trading relationship and acts as a potential constraint on the flow of trade, there also are important economic constraints on trade between the superpowers for the foreseeable future. A review of US-Soviet trade reveals what they are: 1) the volume of US-Soviet trade is minuscule and economically insignificant when compared to America's primary trade challenge of regaining its international competitiveness with its major trading partners, Japan and Western Europe; 2) US-Soviet trade is characterized by a peculiar commodity composition compared to trade between other developed countries; and 3) the flow of trade between the United States and the Soviet Union is unbalanced.

To elaborate on the first characteristic, trade flows between the United States and the Soviet Union are minuscule, compared to trade between other developed countries and compared to the two countries' trade with the rest of the world. Starting in 1972, trade turnover began to increase from the

minimal levels of the 1950's and 1960's, but it has never exceeded $5 billion. In 1987 US exports to the Soviet Union accounted for about six tenths of one percent of total U.S. exports; and imports from the Soviet Union accounted for less than one tenth of one percent of total US imports. By the same token, US trade represented less than four tenths of one percent of Soviet exports to the world and about 1.6 percent of total Soviet imports.

Second, US-Soviet trade has its own peculiar commodity composition, compared to trade between other developed countries. Corn, wheat, and other agricultural commodities have dominated US exports to the Soviet Union. Since 1971, the share of agricultural products in US exports to the Soviet Union has ranged from roughly fifty to eighty-five percent. Only once -- in 1974 -- did agricultural commodities account for less than fifty percent of US exports to the Soviet Union. Starting in 1972, US sales of nonagricultural commodities increased, reaching a peak of $819 million in 1976. Last year, two commodities, corn and wheat, accounted for fifty-two percent of all US sales to the Soviet Union. Nonagricultural exports amounted to $560 million.

A small number of products -- mainly raw materials -- dominate Soviet exports to the United States. In 1987, for example, the top ten Soviet exports to the United States were light fuel oils, rhodium, anhydrous ammonia, palladium, aluminum waste and scrap, sable fur skins, crude petroleum,

semimanufactured palladium, uranium compounds, and heavy fuel oils . These ten products accounted for sixty-seven percent of all Soviet exports to the United States during the year.

Third, the flow of trade between the United States and the Soviet Union is unbalanced. In every year since 1971, the United States has run a surplus in merchandise trade with the Soviet Union.

The relatively low level and unbalanced composition of US-Soviet trade suggest that there is considerable room for trade expansion and diversification. But, projecting the future of US-Soviet trade is a hazardous undertaking. Trade projections are normally based on judgments about the behavior of economic variables such as growth rates, interest rates, and commodity prices. Such variables provide a sufficient basis for projections of West-West trade, but US-Soviet trade cannot be forecast solely on such a conventional basis.

While US-Soviet trade has grown substantially since the Sixties -- from less than a quarter of a billion dollars in 1971 to close to 1.9 billion dollars in 1987, it has followed no steady course. Because politics plays such an important part in shaping the trade pattern between the superpowers, the bilateral trade pattern in the Seventies and Eighties is a matter of two steps forward, one step back. (This up-and-down performance contrasts with the generally upward trend of trade between the Soviet Union and other Western countries during the Seventies and Eighties.) In 1972 and 1973, bilateral trade began to pick up,

exceeding $1 billion for the first time in 1973. But this upward trend was arrested in 1974 when trade turnover slipped below the $1 billion mark. During the next two years, bilateral trade increased dramatically, exceeding $2 billion in 1975 and 1976. Once again, the upward trend was halted; in 1977, trade turnover fell below $2 billion. During the next two years, the trend was upward, and bilateral trade reached its peak of $4.5 billion in 1979. In 1980, however, bilateral trade fell precipitously to less than half its 1979 value. In 1981 and 1982, US-Soviet trade began to recover; trade turnover exceeded $2.5 billion in both years, only to slip below this level in 1983. In 1984, the trend turned upward, and bilateral trade reached $3.8 billion, its second highest level during this period. It fell again to $2.8 billion in 1985 and $1.8 and $1.9 billion in 1986 and 1987, respectively.

When the overall political relationship between the United States and the Soviet Union improves as it did in the early Seventies during the era of detente, bilateral trade tends to increase. Conversely, trade tends to decline when the overall political relationship deteriorates, as it did at the beginning of the Eighties. Political determinants are more important than economic ones in giving the trade relationship its erratic pattern. This is not to say, however, that conventional economic variables can be ignored in projecting US-Soviet trade. Energy prices, Soviet grain production, and exchange rates do influence the level and composition of US-Soviet trade. The Soviet

planning cycle, in which imports of machinery and equipment for major projects rise during the first years of the 5-year plan and fall in the last years, may also be added to the list of economic variables influencing bilateral trade. Even in the context of a favorable overall political relationship, bilateral trade will not necessarily increase if there is no underlying economic basis.

Two Scenarios: Room for Skepticism

There are two obvious scenarios for the future of US-Soviet trade: bilateral trade could remain stable at the relatively low and unbalanced levels of the Seventies and early Eighties. Alternatively, US-Soviet trade could expand significantly along the model of trade between the Soviet Union and other Western countries. Which scenario US-Soviet trade will follow -- steadily expanding or stunted and capricious -- largely depends on political variables. If the improvement in the overall political relationship that began around 1983 is halted, US-Soviet trade is likely to follow the first scenario. Trade flows could even decline significantly.

Many American observers remain skeptical about the possibilities for significantly expanded bilateral trade even in the context of the relatively favorable political climate now prevailing between the two countries. In particular, they raise the question: In what areas are there possibilities for expanded trade? Some skeptics would argue that Soviet prospects for

expanding and diversifying exports to the United States are limited. In their view, the Soviet Union is likely to continue to experience difficulties in expanding non-traditional exports, particularly of finished manufactures. As for Soviet prospects for expanding sales of traditional exports to the United States, they note that U.S. demand for many of these products fluctuates widely according to economic conditions.

Many observers are also skeptical about US export prospects as well. Although most American observers are relatively optimistic about the prospects for grain exports, they note that grain sales are liable to fluctuate widely, depending on Soviet harvests. (Negotiators are still ironing out differences between the annual tonnage minimums of grain that each side can agree on in the new long-term grain agreement. Commentators expect the agreement to last between three to five years, have greater flexibility for averaging out the annual minimum purchase over more than one year, and to average nine million tons a year.)

There is considerably more skepticism about the prospects for non-grain exports. Security considerations have constrained and will continue to constrain US sales of manufactured goods to the Soviet Union, but many American observers predict that other factors could also operate to constrain such sales in the future. For example, the nonconvertibility of the ruble will suppress sales. A key uncertainty is the impact of the economic, bureaucratic, and social reforms now being introduced in the Soviet Union on decisionmaking for trade.

LIMITS ON ECONOMIC LEVERAGE

The limited basis for trade obviously limits the opportunities for leverage. The rationale underlying past attempts to apply economic leverage has been based on Washington's perceptions both of American economic influence and the Soviet Union's economic need for items whose supply the United States could effect. Having tended toward autarky, however, the Soviet Union has carefully avoided developing a relationship in which it becomes economically dependent on another powerful country. When the USSR has entered Western markets, it has stayed for only short periods of time. Furthermore, increased trade with the United States seems to occur at the Soviet's bidding: from 1920 to 1922, when Lenin encouraged foreign investment to develop the Soviet economy; between 1934 and 1938, when the Soviet Union felt compelled to turn from its traditional trading partner, Germany, then under Fascist rule; from 1942 to 1945, when the Soviet Union relied on lend-lease to aid its war effort; in the first two years after World War II, when the Soviet Union used American relief payments toward reconstruction of vast war damage; in 1964, when Russia suffered a disastrous harvest and turned to the United States because Canada was unable to supply the necessary grain; and in the early 1970's, when the USSR suffered another serious harvest failure and its leadership thought Western technology could increase lagging productivity. Soviet-US trade reached an all-

time high in 1979; not coincidentally, this followed another poor Soviet harvest. The requirements of perestroika just may mark the latest example.

Even when the Soviet Union is at a critical economic juncture and heavily reliant on Western products and technology -- which happens rarely and only fleetingly -- the use of economic leverage to obtain political concessions from the Soviet Union does not have a record of great success. America's ability to wield an economic weapon with sureness and subtlety is unquestionably hampered by domestic constraints. Congress and the president may not agree on the best course. Interest groups can hamper execution of policy. American farmers and maritime unions have made the use of grain as a tool of diplomacy an approach fraught with problems. And American businessmen, ignoring the inherent political dimension of U.S. Soviet relations, have traditionally lobbied for trade with no strings attached.

Policy Lessons

Some might conclude that the principal lesson learned from past efforts to tie political objectives to economic concessions -- such as the Jackson Amendment -- is that economic leverage will not work. However, history can be read, for example, to show that the United States received marginal, but recognizable cooperation from the USSR during the 1972 Vietnam peace negotiations. Even in the case of emigration, the Soviet

leadership appeared to adjust its behavior -- first in response to economic concessions extended by Kissinger and Nixon, who gave or promised concessions before Jackson introduced his amendment, and then later to avert the Jackson amendment while it was pending but not yet approved in Congress.

Techniques of Applying Leverage

Determining the success of a given policy of altering Soviet behavior depends largely on what one is trying to accomplish and whether it requires the development of a new policy, a change in leadership, or an alteration in the political nature of the regime. Perhaps small shifts in Soviet policies can be encouraged, but big ones are clearly very difficult.

The manner in which the demands are couched is also very important. If demands are presented belligerently and highly advertised, chances of successfully gaining concessions from a great power like the USSR are less. It may be that using a policy of incentive -- a carrot -- carries less risk and greater chance of success than a policy of denial -- a stick. Moreover, changes in domestic policies may be more difficult to achieve than adjustments in Soviet foreign policy. Accordingly, policymakers should keep the following questions in mind when confronted with the urge to attempt leverage.

1. Are incentives more effective than disincentives?

2. What types of changes are negotiable (changes in Soviet domestic versus foreign policies; long-term versus

short-term changes)?

3. What are the best tactics for presenting demands (secrecy versus public negotiations; bilateral versus multilateral efforts)?

THE UTILITY OF LEVERAGE IN THE 1988 HUMAN RIGHTS CONTEXT

For the reasons described above, the United States may influence the Soviet Union but the Soviets control the tap on emigration and on any other matter of human rights. Taking emigration figures for Soviet Jews as an indicator of human rights compliance, it is clear that the Soviets control the timing and numbers according to their own domestic decision-making. When the Soviets are trying to court Western public opinion for tactical reasons -- for example when ratification of an arms control agreement is pending or access to Western financing or technology is desired -- the number of emigrants rises. The number of Soviet emigrants reached the rate of 32,000 a year in 1972 before the Jackson Amendment was even introduced. It rose marginally to an annual rate of 35,000 in 1973 when the Amendment was pending. It dropped in 1974 to 20,000 -- again while the amendment was pending -- and then dropped further when the Amendment was passed in 1975. There is a closer correlation between the Soviets' desire to court western public opinion coincident to a desire for trade with the West and higher numbers of emigrants than there is between the introduction, pendency, or passage of the Jackson Amendment and higher numbers of emigrants.

Nevertheless, the United States must be very clear what the standards or criteria of desirable behavior are so that when the Soviets do desire to court Western public opinion, it will be clear to the Soviet leadership that human rights compliance including freedom to emigrate is a priority.

Insisting on human rights compliance as a part of the fabric of US-Soviet relations does not stand in the way of trade between the superpowers. Human rights compliance -- and even the existence of the Jackson Amendment in the lawbooks -- is not in and of itself a roadblock to commercial relations with the Soviet Union. If you look at the tiny volumes, the erratic trends, the unbalanced basis of trade, it is clear that there are enough intrinsically economically based barriers to trade that will have to be dealt with before the Jackson Amendment becomes a barrier. Do not forget that the Jackson Amendment provides for a waiver from its sanctions if the President can provide Congress with assurance that Soviet policy is providing for freedom of emigration. Respected leaders of the National Conference on Soviet Jewry, I am told, feel in retrospect that they should have supported a waiver of the amendment in 1979 when the numbers reached the all time high of 51,320. It remains to be seen -- if and when emigration numbers reach that point again -- whether, assuming the waiver is invoked, commercial relations will increase. It is far easier for the Soviet authorities to increase and sustain emigration than it is for them to increase and sustain exports profitably of Soviet manufactured goods into

Western markets.

In sum, I would not exaggerate the utility of leverage -- whether it is a carrot or a stick. There is room for subtle gains here but not crushing victories. And I would not exaggerate the commercial potential of US-Soviet trade. Both superpowers are losing clout relative to the other nations on the globe; the world is moving from a bipolar to a multipolar model. But it would be wrong to underestimate the need for the United States to be clear, consistent and constant in its objectives when relating to the other great superpower of the world. Finally we need our allies to be part of a consistent position. Herein lies of the value of the Helsinki Accords.

In closing, I want to make it clear that while I have dwelled on emigration and the Jackson Amendment as a metaphor for human rights compliance issue, I firmly believe that the United States should not be interested in numbers alone or a single ethnic group alone. Open borders should be our concern -- open for freedom of movement of individuals and goods alike.

APPENDIX V

Written Testimony of Roger W. Robinson, Jr.
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at the National Security Council (1982-1985)

before the
Commission on Security and Cooperation in Europe

on
US - Soviet Trade Relations

May 10, 1988

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Economic and Financial Burden-Sharing

by

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The relationship between U.S. international economic policies and national security is rapidly gaining public prominence and bipartisan Congressional attention. The coordinated adoption and reaffirmation of more disciplined East-West financial policies should become the next major Alliance burden-sharing obligation. The lack of Western public support for increased defense spending to modernize conventional and nuclear forces and maintain an effective global basing structure is a compelling argument for allied cooperation in curtailing the undisciplined financial underwriting of a substantial portion of Soviet global commitments by Western banks. The West can no longer afford to counter the strategic consequences of the continued flow of billions of dollars in untied commercial bank credits to Soviet Bloc borrowers (estimated at over $20 billion in 1986 alone).

Similarly, the Alliance would pay an exorbitant defense price were it to abandon the International Energy Agency (IEA) Agreement of May, 1983 which, in effect, limits Soviet natural gas deliveries to Western Europe beyond those amounts already contracted by year-end 1982 (i.e. a 30% ceiling on the Soviet share of total West European gas supplies). This IEA agreement, endorsed in the Williamsburg Summit Declaration (May 1983) and the NATO Ministerial Communique (June 1983) is projected to cost Moscow roughly $150 billion in foregone hard currency income over a twenty-five year period beginning in the mid to late 1990's. Sustained implementation of the IEA agreement would ensure that constructive economic pressures on the USSR for arms control would remain. The agreement is also preventing the Soviets from eventually commanding a 50-60% share of Western Europe's total gas supplies and the attendant political leverage which would result from such a development.

The uncontested Soviet entry into the international securities markets in January, 1988 is representative of the kind

of strategic set-back the West is now facing as Moscow pursues its ambitious international economic agenda. For the first time, Western securities firms, pension funds, insurance companies, corporations and even individuals are being attracted as new lenders of untied funds to the USSR. Not only does this development open new avenues for Moscow to obtain, over time, billions of dollars in additional general purpose, cash loans, but it potentially recruits politically-influential new constituencies in the West which would have a vested interest in supporting continued economic, financial and even political concessions to the USSR.

The purpose of this paper is to outline briefly proposed Alliance policy prescriptions in the field of economic and financial security, including recommended Western responses to the current and projected Soviet economic policies toward the West.

East-West Finance

I. Achieve an Alliance agreement to phase-out untied, general purpose lending to Warsaw Pact countries and other potential adversaries.

- o Untied loans are loans which are discretionary cash with no underlying trade transactions, projects or jobs. Untied, general purpose lending to sovereign borrowers was one of the four major causes of the current trillion-dollar international debt crisis (i.e. along with the collapse of commodity prices, disinflation, and capital flight) and therefore cannot be justified from a purely commercial perspective. Untied funds are not earmarked for productive purposes, such as export-oriented industries, and hence do not create the expanded economic growth necessary to repay the loans. Ironically, the Soviet Bloc is one of the only group of countries remaining in the world which continue to receive 1970's-style general purpose loans on the syndicated loan market.

- o In 1986, about 80% or $19 billion of the estimated $24 billion in medium term Western commercial bank loans made to Soviet Bloc borrowers were in the form of untied cash credits (not including short-term credits or deposits). The interest rates on 8-10 year loans to the USSR, Bulgaria, and Czechoslovakia were very low compared to terms for LDC borrowers, approximately 1/8th of 1% over the cost of funds (about 7 1/2%).

  -- The next economic summit of the industrialized countries in Toronto should be used to launch a

multilateral initiative to supervise and monitor the voluntary adoption by the commercial banks of more disciplined and transparent Western lending practices with regard to Warsaw pact countries and other potential adversaries.

-- The Organization of Economic Cooperation and Development (OECD) and/or the Economic Committee of NATO are well equipped to supervise such a voluntary initiative and have successfully accomplished the implementation of similar undertakings in the past (e.g. there are at least three major OECD precedents for financial and trade reforms in the 1980's when the US share of the practice in question was marginal or nonexistent).

-- Western commercial banks should eliminate untied credits by: 1) lending only in support of specific trade transactions and projects; 2) matching loan maturities to the duration of the underlying transactions; 3) aggregating and monitoring bank deposits in Soviet Bloc-owned banks, including those located in the West; and 4) applying established project lending techniques to ensure that loan proceeds are strictly dedicated to the project or joint venture in question.

o The US Government should include the untied loan issue and other major East-West economic and financial security policies as central components of all future approaches to our allies (bilaterally and multilaterally) in the area of defense burden-sharing. The multibillion dollar annual savings for US taxpayers in the defense budget which could eventually result from such coordinated economic and financial burden-sharing policies should be underscored.

o Alliance governments should deny the USSR expanded access to the international securities markets because of the potentially damaging consequences to vital Western security interests which result from the diversion of untied Western borrowings by Moscow (e.g. support for client states, funding of Soviet arms sales, KGB activities etc.).

o The allies should reaffirm the OECD agreement reached in 1982 discouraging taxpayer-subsidized terms on government-backed loans to the USSR.

II. Western governments and financial institutions need to substantially upgrade financial data collection and disclosure concerning Soviet Bloc indebtedness and financial flows.

- The Bank for International Settlements (BIS) should close current gaps in Western statistical reporting. For example, inter-German financial flows, presently not reported to the BIS, should be detailed in BIS periodic reviews.

- The BIS should include the estimated $10 billion in Western bank deposits in 100%-owned Soviet subsidiary banks located in the West as part of the total indebtedness of the Soviet Union. (These deposits--which are untied loans--are currently listed as the debt of the Western countries in which the banks are located).

- The BIS should report credit exposure of Western non-banking institutions (e.g. trading companies, securities firms, pension funds etc.) as part of the total indebtedness of the USSR. The same should hold for Western credit exposure to Soviet joint ventures whether in the USSR or third countries.

- The Federal Reserve should collect data detailing all credit exposure to the Soviet Bloc (including deposit placings) of US banks from off-shore branches and subsidiaries, and make the data available for public review.

- The OECD and/or the Economic Committee of NATO should examine the quality and terms of Soviet hard currency loans to Third World countries (estimated to total as much as $65 billion) in order to identify the scale of portfolio problems.

- Western commercial banks should try to ensure that the proceeds of Western bank loans to and deposits with banks of third countries (e.g. the Middle East or Finland) are not downstreamed to Warsaw Pact countries on an unreported basis.

- Western intelligence agencies should monitor, if possible, the accounts of Soviet client states to ensure that the proceeds of Western syndicated credits to Soviet Bloc borrowers (e.g. the German Democratic Republic) are not "skimmed" and downstreamed to those accounts on an unreported basis.

- Western commercial banks should tightly structure loans dedicated to large projects and joint ventures within the Soviet Bloc to ensure that the loans are not, in effect, providing duplicate financing for the project or joint venture in question. For example, in the case of the massive Orenburg gas pipeline project in the USSR during the late 1970s, the Soviet Bloc paid for the Western equipment imports primarily through natural gas deliveries, while the proceeds of the series of Western "project" loans, ostensibly for the same purpose, were largely diverted for other purposes.

- Those involved in data collection should recognize that the uses of Western borrowings and West to East financial flows can be potentially strategic in nature, depending on whether or not the funds are tied to identifiable, peaceful purposes. The Soviets have incentives to divert credits given their shortages of hard currency income. In 1986 the Soviets earned only about $30 billion in hard currency or a little over a quarter of the total sales of General Motors in 1986. In addition, it should be recognized that the temptation for Soviet Bloc diversion of Western borrowings is substantial given the debt-laden status of Cuba, Nicaragua, Ethiopia, Mozambique, Syria, Angola, Afghanistan and Vietnam.

East-West Energy Security

III. The allies should reaffirm the International Energy Agency (IEA) Agreement of May 1983 in the context of economic summitry and NATO ministerials.

- The Soviets reportedly expanded their gas exports to Western Europe by roughly 20% last year and are gradually approaching the 30% ceiling on Moscow's share of total West European gas supplies which is, in effect, embodied in the IEA agreement. Soviet predatory pricing practices could easily undercut the commercial viability of future Norwegian and other more secure Western supplies in the absence of the IEA agreement.

- The recent establishment of an official US-Soviet energy working group has sent an inconsistent signal to our allies concerning US resolve to inhibit Soviet gas exports to Western Europe beyond those amounts already contracted by year-end 1982.

- Japan is under pressure from Moscow to proceed with the $3-3.5 billion development phase of the Sakhalin offshore gas and oil project (i.e. a subsidized joint

venture between Japan and the USSR established in the mid-1970's). Tokyo should be urged to reserve its projected LNG demand in the 1990's and beyond for competitive US supplies, not Soviet or other less secure third country supplies. This would both enhance Asian energy security and help ease our serious bilateral trade imbalance.

- Generally, it should be recognized that the energy sector is the most strategic civilian sector of the Soviet economy, accounting for about 65% of total annual Soviet hard currency income. Any decision by Alliance members and Western companies to assist the extraction, processing, and transmission of Soviet energy resources, particularly for export, would provide potentially enormous assistance to the USSR's hard currency earnings and, in the case of natural gas, could create inordinate Western dependency on Soviet supplies.

National Security Export Controls

IV. Strengthen the Coordinating Committee on Multilateral Export Controls (COCOM).

- U.S. and Western taxpayers are, in effect, penalized billions of dollars annually in additional and unnecessary defense spending to counter the consequences of the illegal Soviet Bloc acquisition of militarily-relevant Western technology. Much of this strategic technology is diverted through third countries.

- COCOM has proved useful in impeding the flow of strategic technology to Warsaw Pact countries. Nevertheless, COCOM's annual budget and institutional capabilities are woefully inadequate given the crucial national security function it performs. The Administration and the Congress need to persuade our allies to increase substantially both of the above and negotiate effective export control agreements with non-COCOM countries.

- The bolstering of enforcement measures is fundamental to the success of COCOM's mandate. The prodigious Soviet effort to illegally acquire and apply strategic Western technology involves billions of dollars and tens of thousands of espionage and technical professionals. The West, in comparison, dedicates a tiny fraction of these massive Soviet resource allocations to curtailing Western sponsorship of Soviet military R&D and hardware requirements.

- Although streamlining and routinely reviewing the COCOM list to avoid unnecessarily impeding Western export competitiveness is important, we should not lose sight of the need to secure greater public understanding and support for a stronger COCOM.

Human Rights and East-West Trade

V. Reaffirm the Jackson Vanik and Stevenson amendments to the Trade Act of 1974.

- The Jackson-Vanik and Stevenson amendments link the granting of equal tariff treatment (most favored nation status) and US Export-Import Bank credits to greater freedom of emigration from the USSR. The amendments have become a symbol of the US commitment to human rights and compliance with the Helsinki Accords and enjoy broad bipartisan Congressional support.

- Any efforts to decouple the linkage between human rights and East-West economic and financial relations should be opposed until the Soviet Union is in full compliance with the Helsinki Final Act.

- During a period when Moscow has an unprecedented need for major Western infusions of capital, equipment, technology, management, distribution and marketing skills, the leverage to advance the cause of Soviet Jews and other ethnic minorities is particularly potent.

Soviet Membership in the International Institutions

VI. Soviet efforts to gain observer status and membership in Western economic and financial institutions should be opposed.

- The Soviets are actively pursuing membership in such institutions as the General Agreement on Tariffs and Trade, the Asian Development Bank, the World Bank, and the International Monetary Fund, in that order. There are three basic reasons why such efforts by Moscow should be opposed:

  -- The USSR has traditionally used its presence in such organizations for disruptive, and propagandistic purposes, often recruiting Third World countries to advance its short-term political goals. Until there is concrete evidence that this kind of behavior has changed, new opportunities should not be presented.

-- The centrally-controlled, command economy of the USSR is fundamentally incompatible with the market-oriented philosophy underpinning these institutions. An irreversible track record of market-oriented economic reform should be present prior to consideration of observer status and membership.

-- The Soviet Union and other Warsaw Pact countries should demonstrate considerably greater compliance with the Helsinki Accords as a precondition to observer status and membership of these organizations.

Eliminate Subsidized Wheat Sales

VII. US sales of subsidized wheat to the USSR should be ended as part of an Alliance effort to eliminate all taxpayer subsidies of trade and financial relations with the USSR.

- It is inconsistent for the Administration to have achieved a hard-fought allied consensus to eliminate subsidies on government-backed credits to the USSR and then itself engage in subsidized wheat sales. The signal sent by this development could easily erode allied willingness to steer away from any subsidies in trade or financial transactions with Warsaw Pact countries.

- Thus far, about 13 million metric tons of US subsidized wheat has been sold to Moscow at an estimated cost of over $500 million to US taxpayers.

- The Soviets are now seeking to have wheat subsidies made a permanent feature of the US-USSR Long-Term Grain Agreement through the insertion of language in the agreement to the effect that "US wheat prices will be competitive with the world price." This is a diplomatic way of saying that any disparity between US wheat prices and the world price will be subsidized by US taxpayers or the Soviets will be under no obligation to buy.

- On occasion, subsidies may be necessary to counter unfair trading practices by the European Community and other suppliers which routinely use subsidies. Nevertheless, the line should be drawn that a "subsidy war" among the allies favoring Moscow will not be permitted.

Executive Branch Reforms

VIII. Establish the position of Undersecretary of Defense for International Economy Security.

- The emergence of economic and financial security as a central underpinning of US national security, requires a high-level institutional focal point in the Administration.

- The occupant of this new position would be responsible for identifying, analyzing, and monitoring the range of issues associated with capital, trade, and energy flows primarily between the Free World and potential adversaries.

- The Undersecretary of Defense for International Economic Security would prepare policy recommendations for the President and the Cabinet on strategic dimensions of international economic and financial relations, including security-related issues outside of East-West relations, such as the international debt crisis.

- The absence of such a position in the Executive Branch risks the continuation of sporadic, ad hoc attention to this crucial family of issues. For example, how is it possible that the US policy-making community has never systematically analyzed and debated the central question of how the Soviet Union funds itself and its global activities?

IX. Reestablish a Cabinet-level Senior Interdepartmental Group-International Economic Policy (SIG-IEP) under the auspices of the National Security Council.

- Between July 1982 and April 1985, the SIG-IEP successfully integrated overarching US national security and foreign policy goals in the formulation of international economic policy.

- The competing and often contrary views of the relevant government agencies were either reconciled at the Cabinet level or accurately translated into options for the President's decision, in the context of his broader foreign policy objectives.

- The prominent role of the US security community helped ensure that economic and financial security policies received proper priority on the President's agenda. Regrettably, under the current Economic Policy Council, the roles of Defense, the CIA and the NSC have been diminished.

Conclusion

The suggested policy prescriptions and Western responses to Soviet economic overtures outlined above are specifically designed not to impede the expansion of nonstrategic East-West trade and finance. Implementation of these recommendations on the security aspects of economic and financial relations would substantially reduce Soviet flexibility with regard to financial and technology diversions and could result in multibillion dollar defense-related savings annually for Western taxpayers.

Reforms in East-West trade and finance could even advance prospects for arms control. The Soviets would have a greater incentive to make the kind of positive trade-offs between their military and civilian economies that we are hopeful of seeing in the context of perestroika. Thus far, there is no evidence that Gorbachev's economic reform program is resulting in the reduction of the Soviet military sector's share of Soviet GNP. Indeed, the intelligence community has recently estimated that Soviet defense spending as a share of total GNP increased in 1987.

Most Alliance countries have acknowledged the effectiveness of the technique embodied in the words "follow the money" to identify and locate drug traffickers, organized crime figures, inside-traders, espionage agents, and international terrorists. In meeting the Soviet challenge, it is troubling that the same kind of investigatory tool has not been more vigorously applied as a major component of our most vital Alliance security policy. The growing bipartisan consensus in the Congress on the untied loan issue and the heightened interest on the part of the US security community, human rights groups and organized labor in East-West economic policy reforms, indicate that economic and financial burden-sharing with our allies has come of age for the 1990's and the twenty-first century.

APPENDIX VI

COALITION TO FREE SOVIET JEWS
Representing concerned organizations in New York City, Long Island, Westchester, Rockland and Bergen Counties

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Alan D. Pesky, Chairman
Coalition to Free Soviet Jews

Testimony to the U.S. Commission on
Security and Cooperation in Europe

Hearing On East-West Trade
May 10, 1988

I am pleased and honored to submit testimony to the Commission on the critical issue of U.S.-Soviet trade. The trade issue currently represents a confluence of several important factors and goals. As such, bilateral trade can -- and I suggest must be -- central to our efforts to promote both human rights and increased cooperation, particularly as outlined in the Final Act.

It has long been an open secret that the economy of the Soviet Union was faltering, causing the Soviets to fall further behind the Western industrial nations and even, eventually, the emerging industrial nations. Under Mikhail Gorbachev this fact has not only become part of Soviet public debate, it is the central premise of the economic restructuring program of perestroika.

A major tenet of the perestroika program involves increased trade with the West and its necessary corollary: a substantial change in the overall trade relationship between

the Soviet Union and the industrialized West, particularly the United States.

In this effort, the Soviets have taken a number of steps: they have become increasingly vocal about their objections to trade barriers, they have begun an ambitious effort to court American businesses to partake in joint-venture projects, and finally, they have voiced interest in participation in Western trade institutions from the narrowly focused Multi-Fiber Agreement to the more broadly empowered General Agreement on Trade and Tariffs (GATT) and the International Monetary Fund (IMF). The Wall Street Journal summed up this effort well when they wrote of the Soviets, "They may not believe in capitalism, but they sure know how to use it."

Part of the Soviet campaign included a rousing speech by General Secretary Gorbachev to an estimated group of 500 U.S. business leaders brought to Moscow by the U.S.-U.S.S.R. Trade and Economic Council last month. Thus far, only a handful of solid commitments have been made and prospects for a wave of joint-ventures seem unlikely for the immediate future. But it is not surprising that the vast potential market that the U.S.S.R. represents has sparked the initial interest of American business.

There are a number of important factors that impede the growth of U.S.-Soviet trade. Many of these factors focus on economic and bureaucratic matters. But foremost among the issues at the axis of an improved U.S.-Soviet trade relationship is the

political cast of bilateral relations. In the final analysis, regardless of whatever obstacles exist or are removed, bilateral trade and commerce rests on the political relationship between the superpowers. In this regard, Soviet policies on human rights and Soviet Jewish emigration are central. The linkage between trade and human rights is both a barrier and a potential bridge to increased commerce.

The 1974 Jackson-Vanik Amendment links U.S.-Soviet trade to human rights by denying communist countries Most Favored Nation (MFN) trading status until they permit substantive and sustained emigration. Other examples of legislation that control U.S.-Soviet trade are found in the Byrd and Stevenson Amendments, which limit Export-Import Bank credits to the Soviet Union. As well, there are administration controls on business with the Soviets used to protect national security and advance foreign policy interests.

The Soviets, in seeking U.S. trade, have privately voiced particular interest in gaining Most Favored Nation status. While some here have suggested MFN would have little impact on Soviet trade, Gorbachev's chief economic advisor, Abel Abanbegyan, believes that with the drastically lower tariffs under MFN, the U.S.S.R. could double its exports to the U.S. In addition, MFN represents a politically symbolic goal for the Soviets that would enhance their perceived stature. MFN status could aid the Soviets in their efforts to join the IMF and GATT. As well, the Soviets

would greatly benefit from the trade credits they are currently denied under Jackson-Vanik and Stevenson.

Equally important, the human rights trade restrictions represent the potential for political instability in the U.S.-Soviet relationship, creating risk to business ventures that is anathema to those contemplating trade with the Soviets. As a recent New York Times article noted, many businesses that dealt with the Soviets in the 1970's were hurt when relations turned sour following the Soviet invasion of Afghanistan.

The potential removal of human rights trade restrictions would have the broad effect of signalling a more stable and fertile era for bilateral commerce. Such a watershed in relations would enhance prospects for both the Soviets and U.S. business.

To gain these important advantages to their perestroika program, the Soviets must simply normalize their emigration process, allowing Soviet Jewish emigration to reach significant levels. Without substantive progress and increased compliance with commitments under the Final Act, particularly in the area of religious and cultural freedom, Jackson-Vanik and other trade restrictions will stay in place.

The linkage concept is an important parallel to the linkage of Baskets II and III under the Final Act. The maintenance of the linkage concept is critical to the efficacy of the Helsinki Accords and ultimately, to fulfillment of human rights principles. The linkage concept and the construction of the Helsinki baskets

require equivalent progress within the different spheres of relations. While Soviet progress on human rights is still partial at best, it would be inappropriate and counter-productive to actively encourage significant changes in the bilateral trade relationship.

Efforts to promote trade and commerce without consideration for human rights, give the Soviets a meaningful incentive to ignore their human rights obligations. If the United States allows bilateral trade to increase in the absence of progress on emigration and other rights issues we signal to the Soviet Union, the other Helsinki signators and the world that our human rights advocacy is no more than rhetoric and that the linkage concept exists only in the halls of Helsinki review conferences.

In addition, it is naive to believe that increased trade without an equivalent increase in Soviet human rights compliance would serve U.S. commercial or business interests. Any trade relationship with the Soviet Union that rests on a political relationship bereft of substantial progress on human rights is unstable and will either inhibit business ventures or, in the longer term, lead to disappointing or damaging results.

The strength of the linkage concept, however, creates a palpable incentive for the Soviet Union to move forward on human rights matters. In light of existing and maintained linkage, as well as Soviet economic goals and needs, an effective way -- perhaps the most effective way -- for the Soviet Union to open up

the U.S. market, facilitate commerce and signal a new era in bilateral trade and relations generally, would be to move comprehensively on the issue of Soviet Jewry.

For those committed or even interested in expanded bilateral trade, human rights progress is crucial to the development of a predictable and profitable environment in which significantly increased commerce could be sustained.

In conclusion, we believe that while linkage should not be removed unilaterally, neither should it be withheld absolutely. At this propitious time, let us use linkage as a salient incentive to the Soviets, emphasizing the extent to which the goals of perestroika are entwined with the need for more and real glasnost. By maintaining and utilizing strong linkage we not only encourage human rights progress, we serve the interests of an enlarged and viable trade relationship as well as the principles to which the United States committed itself under the Helsinki Final Act.

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